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RMD.N - Q4 2023 Resmed Inc Earnings Call

EVENT DATE/TIME: AUGUST 03, 2023 / 8:30PM GMT

OVERVIEW:

Company Summary

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PRESENTATION

Operator

Hello, and welcome to ResMed's Fourth Quarter Fiscal Year 2023 Earnings Conference Call and Webcast. (Operator Instructions) As a reminder, this conference is being recorded. It's now my pleasure to turn the call over to Amy Wakeham, Chief Communications and Investor Relations Officer. Please go ahead, Amy.

Amy Wakeham - *ResMed Inc. - Chief Communications & IR Officer*

Great. Thank you so much, Kevin. Hi, everyone, and welcome to ResMed's Fourth Quarter Fiscal Year 2023 Earnings Call. This call is being webcast live, and the replay will be available on the Investor Relations section of our corporate website later today, along with a copy of the earnings press release and the presentation, both of which are available now. On the call today are Chief Executive Officer, Mick Farrell; and Chief Financial Officer, Brett Sandercock. Following our prepared remarks, Mick and Brett will be joined by Rob Douglas, our President and Chief Operating Officer; and Lucile Blaise, President of our Sleep & Respiratory Care business for the Q&A portion of the call.

During today's call, we will discuss several non-GAAP measures. Please review the supporting schedules in today's earnings press release for a reconciliation of the non-GAAP measures to our GAAP reported numbers. Our discussion today will also include forward-looking statements including, but not limited to, expectations about our future financial and operating performance. We believe these statements are based on reasonable assumptions. However, our actual results could differ. Please review our SEC filings for a complete discussion of the risk factors that could cause our actual results to differ materially from any forward-looking statements made today. I'd like to now turn the call over to Mick.

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

Thanks, Amy, and thank you to all our shareholders for joining us today as we review the results of our June quarter, the last quarter of our fiscal year 2023. Our results reflect incredible growth across our entire business, with double-digit growth in our devices, masks and software businesses. Unconstrained availability of our market-leading cloud-connected flow generator platforms has enabled us to continue to offer access to 100% cloud-connectable AirSense 10 flow generator devices in all of our major global markets and beyond. In parallel, we are ramping up and improving the availability of our best-in-class AirSense 11 platform, which will gain further geographic regulatory approvals throughout the fiscal year and steadily increasing supply also throughout the fiscal year 2024 and beyond. Although challenges within the post-COVID supply chain haven't completely been mitigated yet, we expect ongoing steady improvement in component and end product supply in the quarters ahead using a combination of AirSense 10 and AirSense 11 platforms.

While we remain focused on scaling production and global availability of the AirSense 11 platform, we remain on allocation for the Air 11 platform for the next few quarters. But I want to be clear on this point. With combined availability of the unconstrained Air 10 platform, we have enough devices to meet all of the customer needs that we see in major markets and globally. With the powerful combination of the Air 10 and the Air 11 platforms, we have the 2 best device platforms on the market. Our strong double-digit 23% year-over-year growth in the devices category demonstrates that customers are choosing ResMed, and we are delivering. Our masks and accessories business also performed at a very strong 18% growth in constant currency this quarter. Patient demand continues to drive increased adoption and utilization of our mask resupply programs, augmenting a steady cadence of new patient setups. We continue to see strong growth in both the U.S. business, where provider resupply programs have augmented growth, and in our markets outside the U.S., where our consumer outreach and subscription programs are also driving mask replenishment directly with those end-user patients.

Our teams continue to work incredibly hard to achieve these strong growth results amid a challenging industry environment where component costs and freight costs are still working their way through our inventory post this supply chain crisis. I'm proud of the work that 10,000 ResMedians have put in every week, every month, every quarter to deliver these incredible results for the business, for our customers, for our shareholders and ultimately for our most important customer, our patients. Let's now briefly review updates on the top 3 strategic priorities for our company: number one, to grow and differentiate our core sleep apnea and respiratory care business; number two, to design, develop and deliver market-leading medical devices, as well as digital health solutions that can be scaled globally; and number three, to create, innovate and grow the world's best software solutions for care delivered outside the hospital, a field that we call residential medicine.

In terms of our patient-facing digital health platforms, adoption continues to go very well. The feedback we hear from patients and health care professionals remains very positive. We are seeing strong adoption of the myAir patient app by folks using AirSense 11. In fact, it is more than double the adoption rate that we saw with our AirSense 10 platform, with many, many millions of patients signing up and engaging daily on their myAir app to view their own sleep data on their own phone and to review their own therapy data. This is important, as engagement with the digital health platform like myAir is directly linked to higher adherence to therapy in patients, and higher adherence to therapy is directly related to better patient outcomes to increase resupply and to better economics for the payer and the health care provider, with lower overall health care costs.

Last month, we announced and closed the acquisition of Somnoware. Somnoware is a U.S.-based leader in sleep and respiratory care diagnostics software and physician management software. As part of our ongoing efforts to improve and streamline the end-to-end pathway for patients and make it easier for sleep labs and physicians and their practices to diagnose and manage patients, we're excited about this acquisition that complements our current ecosystem of software solutions, including AirView for providers and physicians and Brightree for home care providers. These ecosystem together will drive greater efficiency and better patient care by accelerating the pathway to therapy and with a better overall customer experience.

We're also excited about our progress across several digital health technology initiatives to further increase the value proposition for our connected health care ecosystem. Over the next several quarters, we plan to introduce several artificial intelligence-driven data products and capabilities on both the physician- and provider-facing AirView platform, as well as the patient-facing myAir app. Early testing of these AI-driven data products is very positive in both of these customer groups, and we will refine to the optimal digital design, and then we will launch, and then we will scale these products around the world. These AI-driven data products provide personalized suggestions to increase therapy adherence and to ultimately improve patient outcomes, as well as patient, physician and provider experience. We will continue to invest in the world's largest digital health

care ecosystem that we have with over 15.5 billion nights of medical data in the cloud as we continue to unlock value from those data to benefit physicians, providers, payers and patients.

We saw strong growth in our Respiratory Care business in the quarter through ongoing adoption of our noninvasive ventilators, as well as our life support ventilator solutions. We're still in the early stages of market development with some of our newer-to-market technologies in this category, including home-based high-flow therapy that we call HFT for treating chronic obstructive pulmonary disease, or COPD, in the home. We continue to generate clinical evidence and economic outcomes to support broader adoption of these technology innovations for treating lung disease in the home. We're encouraged by the clinical results we've seen with our HFT trial so far, and we continue to remain very focused on addressing COPD as one of the top diseases globally for hospitalization and the #1 cause of rehospitalization in the U.S. geography. The prevalence of respiratory insufficiency due to COPD, as well as respiratory insufficiency due to neuromuscular disease, continues to increase, and we are focused on having low-cost, high-quality solutions to address this health epidemic.

Our SaaS business had another great quarter with year-over-year growth of 34%. Our SaaS business growth was supported by another full-quarter contribution from our fast-growing MEDIFOX DAN business, as well as solid organic growth of 8% across our Brightree and MatrixCare portfolio of SaaS businesses. We're pleased to see sustained high single-digit growth in our SaaS business on an organic basis, driven by the ongoing strength in the HME and Infusion segment and more stability in the Facilities segment as patient flows have now rebounded post-COVID.

I'm very impressed by the leadership of our most recent SaaS portfolio addition, MEDIFOX DAN, which is on track and meeting or beating our expectations. I'll be visiting personally with the team in Hildesheim, Germany this quarter to discuss the growth face-to-face with the digital health innovators there in Hildesheim who are changing health care and taking care of people in the lowest cost, lowest acuity and highest quality of life setting, which is very often the home. We believe this is the future of health care, and that's where we're investing and that's where we're winning.

Our customers continue to see the value of adopting technologies to improve and optimize business efficiencies and personalized care, and we deliver the best software solutions to help customers do just that. There is pent-up demand for technology investments in residential medicine verticals, particularly as staffing shortages continue to impact the industry, particularly in nursing, but across the clinician and provider groups. This presents opportunities for ResMed's SaaS solutions to streamline operations and create workflow efficiencies so our customers' staff can focus on providing personal care. It's up to us to deliver for our customers and drive growth. I have confidence that our SaaS business can accelerate from these high-single digits on an organic basis to double-digit growth on an organic basis in the mid- to long-term.

Our SaaS business remains an integral part of ResMed's group growth strategy. This business complements the market-leading software and device solutions that we have in our core sleep apnea and respiratory care businesses. As an important example, our Brightree resupply program continues to demonstrate strong synergies between SaaS and our core business, providing resupply for patients with sleep apnea, COPD, neuromuscular disease and beyond. The output of this work can be seen in our very healthy 19% growth in mask revenues in the U.S. geography this quarter. Ultimately, this work results in better outcomes for the patient, the physician, the provider and the payer, with lower overall health care costs. We are well-positioned as the leading global strategic provider of SaaS solutions for residential medicine globally, and we have created a differentiated value for our customers, as well as long-term sustainable growth for our stakeholders.

Here at ResMed, we are transforming respiratory medicine and residential medicine at scale, leading the market in digital health technology across our businesses. As we continue to scale and drive efficiencies in our operations in this post-COVID world, we continue to leverage appropriate pricing and cost reductions to drive accelerated growth in our bottom line. We are focused on driving top-line revenue and maintaining tight discipline and increasing efficiencies so that we can lower costs and ultimately so that we can accelerate our impact and our bottom-line profitability, delivering even further value for all of our shareholders.

As we move through fiscal year 2024, I see improvements in our business margins with geography mix, with product mix and specifically with strong bilevel and noninvasive ventilator growth, with strong mask growth, and with increased software solutions growth. All these business lines are margin accretive to our group. I also see that the higher inventory costs and freight costs that we've seen through the supply chain crisis continue to work their way through our sold products. And as we progress through the fiscal year, we will continue to drive the transition to AirSense 11, and we will gain regulatory approvals, and we will scale production. All these factors above lead to tailwinds for the gross margin and the net

margin of our business as we move through the fiscal year. I can tell you we are working furiously to drive all of the above elements with our global teams.

We now have over 15.5 billion nights of medical data in the cloud as I said earlier, and those data come from over 21.5 million, 100% cloud-connectable medical devices on bedside tables in 140 countries worldwide. We continue to lead the industry in digital health, and we don't plan to stop anytime soon because there's so much opportunity ahead of us. 7% of our revenues go straight into R&D to power our hardware and our data innovation engines. ResMed's mission and key goal remains crystal clear. We will improve 250 million lives through better residential health care in 2025. This patient-centric mission drives and motivates ResMedians every day. We made excellent progress towards that inspiring goal over the last 90 days. And during the trailing 12 months, we have improved over 160 million lives with the delivery of a complete device platform to a patient or a complete mask system to a patient or a digital health software solution that is helping each person to sleep better, to breathe better and to live a high quality of life with health care delivered right where they live.

As we start fiscal year 2024 here, I'm very excited about the opportunities in front of us. We just had our SaaS ASM earlier this week, and I'll be attending the Country Market Group, CMG group, for our North America team in the coming weeks and sales meetings that are happening around the world. We're on a good trajectory. We have an exciting pipeline. In closing, I want to express my sincere gratitude to the more than 10,000 ResMedians for their perseverance, their hard work and their dedication, both today and every day. With that, I'll hand the call over to Brett in Sydney, and then we'll move and open up for Q&A for the group. Brett, over to you.

Brett A. Sandercock - ResMed Inc. - CFO

Great. Thanks, Mick. In my remarks today, I will provide an overview of our results for the fourth quarter of fiscal year 2023. Unless noted, all comparisons are to the prior year quarter.

We had strong financial performance in Q4. Group revenue for the June quarter was \$1.12 billion, an increase of 23% on a headline basis and in constant currency terms. Revenue growth reflected the ongoing combined availability of cloud-connected AirSense 10 and AirSense 11 sleep devices to support strong underlying global demand, as well as solid growth across our broader product portfolio. Year-on-year movements in foreign currencies negatively impacted revenue by approximately \$3 million in the June quarter.

Looking at our geographic revenue distribution, excluding revenue from our Software-as-a-Service business, sales in U.S., Canada and Latin America countries increased by 25%.

In constant currency terms, sales in Europe, Asia and other markets increased by 14%. Globally, in constant currency terms, device sales increased by 24%, while masks and other sales increased by 18%.

Breaking it down by regional areas, device sales in the U.S., Canada and Latin America increased by 30% as we benefited from strong demand and, as previously mentioned, our continued ability to fully supply the market with combined availability of AS 10 and AS 11 cloud-connected devices. Masks and other sales increased by 19%, reflecting growth in resupply and new patient setups. In Europe, Asia and other markets, device sales increased by 15% in constant currency terms, again reflecting strong demand and improving availability of cloud-connected devices. Masks and other sales increased by 14% in constant currency terms, reflecting increased patient setups.

Software-as-a-Service revenue increased by 34% in the June quarter, reflecting the contribution from our MEDIFOX DAN acquisition and continued strong performance from our HME vertical. Excluding our MEDIFOX DAN acquisition, SaaS revenue grew by 8% in the June quarter. MEDIFOX DAN contributed revenue of \$27.3 million for the June quarter, consistent with our expectations at the time of the acquisition.

During the rest of my commentary today, I will refer to non-GAAP numbers. We have provided a full reconciliation of the non-GAAP to GAAP numbers in our fourth-quarter earnings press release. Gross margin declined by 200 points to 55.8% in the June quarter. The decrease primarily reflects component cost increases, warranty and manufacturing-related cost increases and product mix shifts due to the significant increase in sleep device sales, partially offset by increases in average selling prices. On a sequential basis, unfavorable foreign currency movements accounted

for the 30 basis point decline in our gross margin. And we saw a lower-than-expected product mix benefit as we continue to see strong growth in sleep devices in the U.S. market.

Moving on to operating expenses, SG&A expenses for the fourth quarter increased by 25%, or in constant currency terms increased by 26%. The increase was predominantly attributable to increases in employee-related costs, marketing and travel expenses, as well as the incremental SG&A expenses associated with MEDIFOX DAN that we acquired in November 2022. SG&A expenses as a percentage of revenue was 21.5%, compared to 21.1% in the prior year period. Looking forward and subject to currency movements, we expect SG&A expense as a percentage of revenue to be in the range of 20% to 22% during fiscal year '24. R&D expenses for the quarter increased by 21%, or, in constant currency terms, increased by 23%. R&D expenses as a percentage of revenue was 7%, consistent with the prior year quarter. Looking forward and subject to currency movements, we expect R&D expenses as a percentage of revenue to be in the range of 7% to 8% during fiscal year '24. Operating profit for the quarter increased by 13%, underpinned by strong revenue growth, partially offset by a lower gross margin.

Following the acquisition of MEDIFOX DAN, our net interest expense for the quarter is \$15 million, and we expect interest expense to be a similar amount per quarter in the first half of fiscal year '24. Our effective tax rate for the June quarter was 18.3%, compared to the prior year quarter rate of 17.6%. Looking forward, we estimate our effective tax rate for the fiscal year '24 will be in the range of 19% to 21%. Our net income for the June quarter increased by 7%, and non-GAAP diluted earnings per share also increased by 7%. During the quarter, we incurred \$1.8 million in acquisition expenses associated with our Somnoware acquisition, and we recognized restructuring costs of \$9.2 million associated with the closure of the Aria lymphedema business and workforce rationalization in our German and SaaS business verticals. We also recognized a gain of \$20.2 million within other income in relation to a business interruption insurance claim. These have all been treated as non-GAAP items in our Q4 financial results.

Cash flow from operations for the quarter was \$237 million, reflecting solid underlying earnings, partially offset by a modest increase in working capital. Capital expenditure for the quarter was \$34 million. Depreciation and amortization for the quarter totalled \$47 million. We ended the fourth quarter with a cash balance of \$228 million. At June 30, we had \$1.4 billion in gross debt and \$1.2 billion in net debt, which mainly reflects the funding of our MEDIFOX DAN acquisition. During the quarter, we reduced our debt by \$145 million. At June 30, we had approximately \$745 million available for drawdown under our revolver facility, and we continue to maintain a solid liquidity position. Our Board of Directors today declared a quarterly dividend of \$0.48 per share, representing an increase of 9% over our previous quarterly dividend and reflecting the Board's confidence in our operating performance.

Going forward, we plan to continue to reinvest in growth through R&D and expect to deploy further capital for tuck-in acquisitions, such as our recently announced acquisition of Somnoware, a company that provides an upstream diagnostic management platform that is complementary to our current AirView and Brightree solutions. And with that, I will hand the call back to Amy.

Amy Wakeham - ResMed Inc. - Chief Communications & IR Officer

Great. Thank you, Brett, and thank you, Mick. Kevin, I'd like to go ahead and turn the call back over to you to provide the instructions and run the Q&A portion of our call.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question today is coming from Matthew Mishan from KeyBanc Capital Markets.

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

Mick, with the devices number sort of steady sequentially around the \$600 million mark, is this where the number would kind of base out if you are supplying the majority of the market? And kind of from here, are we looking at just saying \$600 million and then add on some percentage of what this -- the underlying sleep market is kind of growing at?

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

Yes. Thanks for the question, Matthew. And it's a good one. It's hard to predict because there are so many factors involved that are going on in the market right now. But yes, as you said, a very solid number, \$602 million in global devices in the quarter and 30% growth in U.S., Canada, Latin America, 15% growth in Europe, Asia and rest of the world. Look, we're seeing a strong sort of mid-single-digit level of patient flow into the channel. We're seeing in addition to that -- like in terms of new patients, we're seeing in addition to that resupply of patients at that 5-year point for most U.S. reimbursement and various points in the other 139 countries where people make their own decisions or insurance has other criteria to drive that. So it's new patient setups. It's resupply setups. And there's, of course, the impact of a competitor recall, which is -- was supposed to be over in June 30 and now has no definitive date.

And so as we look to that with all those unknown factors, it's very hard for me to say, Matthew, that it's just stop and steady growth from here. It might be stronger growth from here, and that makes it hard to predict gross margins because as we grow the CPAP and APAP numbers so well in the U.S. geography, it's incredible great revenue and cloud-connected and links us with the patients' life, but it is lower gross margin in our group. And so it's great gross profit dollars, but has an impact on our gross margin as you saw that steady apart from FX moving it down 30 basis points. So a complex equation. But I'd say it's at minimum stage where it is and grows with the market, but it could potentially grow above that as we continue to take share and solidify that share through our digital ecosystem. Thanks for the question, Matthew.

Operator

Our next question today is coming from Margaret Kaczor from William Blair.

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

I wanted to follow up first on the competitive dynamic to the extent that you'll -- you see anything maybe in to -- in the marketplace. So whether your key competitors coming back, either approaching or maybe hiring processes, marketing campaigns, anything that maybe they're gearing up for that you're seeing? Or is demand relatively similar to what you've seen in the past, no real change?

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

Yes. Thanks, Margaret, and welcome back. I think it's difficult to predict exactly where they're at from those sort of early emerging signs as you say. Look, we have regional competitors in Europe that we are fighting with every day there, and we have regional competitors in Asia that we're fighting with every day, and regional competitors in the Americas that we're fighting with every day. When Philips comes back, they'll have to start at position #4, if you like, in new patient setups. We are -- they are back, and we are competing with them in some countries in Europe, like in Spain, they never went away because they never had a foam device there. So they've been there the whole time through this recall, and we've been beating them handsomely there. And there's other markets in Europe where they've started to come back, we're competing and winning and maintaining share and growing share. I think the reputation here and the time to market is going to be a very slow progress for them country by country, whether or not they get a consent decree in the largest geography. And so we look at it going forward and say, look, do we have enough supply to take care of all the market demands between us and the other regional players, and we finally got there where I can say that this quarter that we're there and we can take care of it.

So it's almost irrelevant to us how and when in terms of what that looks like because we're able to take care of all the market growth. So for us, it sort of takes away that uncertainty and allows us to push forward. But yes, we're competing head-to-head with them in some -- many countries in

Asia and some countries in Europe, and it's like it was in 2019, where our smaller, quieter, more comfortable, more connected and more digital solutions are taking share and holding share. And it's an ongoing competitive game. And as I said, we're launching some of these AI-driven products on top of this ecosystem. It's an exponential game when you think about digital, and we're well ahead. We've had 2 or 3 years here to sprint ahead, we were ahead before that. And I think it's a long-term game. Won't get -- we'll keep productively paranoid, but we are improving outcomes. We're lowering costs, and the physicians like the workflow efficiencies, and patients like the increased adherence, and payers like the fact that there's an ROI in lowering total health care costs.

Operator

Your next question is coming from Anthony Petrone from Mizuho Group.

Anthony Charles Petrone - Mizuho Securities USA LLC, Research Division - MD & Senior Medical Devices, Diagnostics and Therapeutics Equity Research Analyst

Congrats on a strong top line here, share gains. Maybe a 2-part question, Mick. One would be just on the amount of resupply that's now coming in as it relates to the share gains that you've seen over the past 2 years is the resupply number we're seeing now, where we're actually starting to see consumables come off of the new sockets that you gained. So that would be question one. And then question two, there's obviously the debate out there on GLP-1s. Maybe from the perspective of ResMed, how do you see the GLP-1 phenomenon playing out in the sleep space? Specifically, do you expect to gain more patients from GLP-1s versus maybe certain patients that would fall out of the funnel?

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

Yes. Thanks, Anthony, and welcome back to you, too, to the ResMed following us here. I'll take both your questions and your follow-up in order. So firstly, on resupply, as you know, you've been following us for a number of years. It's not a lock and key. You can use our mask on others' devices and you can use other masks on our devices. The way that we've won market share and nobody has been on a major in terms of not being able to sell recall out there on this. And so we've had head-to-head competition with all the top 5 players in masks these last 3 years, and we've gained really good share with that. So I think it's just the smallest, the quietest, the most comfortable, the minimal size ones, the ones that have full freedom and the ones that have the ability to -- for prone sleepers and side sleepers to provide that capability. And so that's how we've gained share in the mask side and maintained that share. So there is a better together in that when you have an AirSense 10 or an AirSense 11, the mask leak data are more accurate. The interoperability of an AHI calculation or a leak calculation are more accurate. So we certainly push that angle, and we do get some extra share through the device, but it's not as material as the fact that the masks themselves are just excellent, which I think speaks to the sustainability there.

So that strong resupply, as you said, 19% growth in the U.S. 14% growth in Europe, Asia and beyond, where we don't have that sort of automated resupply that we have with Brightree resupply solutions in the U.S. That's been from hard work from our teams in Asia, Latin America and Europe on patient outreach, subscription programs and connecting directly to that end user. So I think post-COVID, people care about respiratory health, respiratory hygiene, and taking care of themselves outside the hospital, and we've been able to leverage that trend in the consumer side as well. So I think it's sustainable, and I don't think -- although may be catalyzed somewhat by our increased device share, I think our mask share is on its own extraordinary due to the intrinsic products.

The second question around GLPs. Yes, look, there's a lot of moving parts. I was just reading in the press today that many U.S. employers are banning coverage of GLP-1s due to cost. European governments have all said, no, from the government insurance side. These things are incredibly expensive, about \$1,000 -- well, it's anywhere from \$800 to \$1,200, \$1,000 a month. So I think there are 3 factors that will mitigate GLPs in the space. One is cost. Two is adherence, and three is side effects. I'll take them really quickly in order. If you look at cost, take a 40-year-old person who's on therapy, full-time, for 40 years, 40 x 12 x \$1,000 is \$480,000 lifetime cost for that patient on a GLP-1 from 40 to 80 lifetime cost. If you take that same patient and say, well, let's treat them with CPAP, right? First year, maybe \$1,000 and then 39 years of -- let's take a really strong case where you get 4 masks a year, and they're all full face masks. That's \$13,500. So it's 35x more expensive to go with the GLP-1. It's just like what's the ROI here? So that's cost. On adherence, the data out there -- about 33% adherence at 1 year through the clinical trials on GLP-1s. That's incredibly low. We get 87%

adherence in 90 days, and we hold it pretty strong there. So I think adherence is a big deal. And third is side effects, reading thyroid, pancreas, kidney, cancer, these major side effects and minor ones like nausea, constipation and pain. Our biggest side effect as President Biden had a little mark on his face, and he was asked about it and it was from his CPAP. Look, I think it's a long road to play out here. I think it's frankly good marketing around the area of obesity, and it can drive patients into the funnel. But I don't think it's going to be a major impact on patients because we've got 936 million of them worldwide, and we need them to get into the funnel. If they come in the funnel because they tried a pill and it didn't work, that's good for us, too.

Operator

(Operator Instructions) Our next question is coming from Suraj Kalia from Oppenheimer.

Shaymus F. Contorno - Oppenheimer & Co. Inc., Research Division - Research Analyst

This is Shaymus on for Suraj. So we saw GM, gross margin, stepped down a little bit. I know you said there were some reasonings for it. But I just -- looking forward kind of in the future, can you maybe you can walk us through the temporary and more structurally permanent changes we should think through as far as GM outlook is concerned?

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

Yes. Thanks for the question. And look, it's a good one. Lots of factors going on gross margin. Actually, the major one, as you noticed, sequentially on the 30 basis points, was foreign exchange. And that was on inventory as it flowed through our funnel as we sold both CPAPs, APAPs, we had FX that had impacted 6, 9 months ago, but they're flowing through inventory that we sold during the June quarter. That was the headwind of 30 basis points from Q3 to Q4. Look, I think there's so many moving parts. But when you add it up and you look at geography mix and the upside opportunity for us to grow our business in Europe, Asia, particularly Japan, which has some chance for acceleration over the coming years; product mix, I mentioned in the prep remarks, particularly on bilevel and our noninvasive ventilator growth. So think AirCurve ST, ST-A, AirCurve ASV. And our mask side, particularly the full face, but any of the masks, all of those are gross margin accretive to our group. And I see opportunities for strong growth in all those categories.

And also our software solutions have gross margin accretive capabilities. And as we go on an organic basis from single digits, to high single digits to low doubles there on the software SaaS side of the business, I think that's margin accretive. So I feel good about that.

I also know that we're working through the sort of higher inventory costs that we had in that supply chain crisis. We had to spend more on chips, parts and pieces in those contracts and get more expensive components for the cloud-connected chip and beyond. And those freight costs that we invested in and everyone's talking all the news the freight costs are down, you should take away your surcharge. Well, no, actually, the freight costs that we paid 6, 9 months ago are working their way through our gross margin, as you saw in the June quarter, and that will go on for some time. But that's going to continue to go down over time. And as that does go through, our sold products, there's going to be some tailwinds for gross margin.

And the final one and really important one is we're going to drive AirSense 11. It's the best in the world product. It's better than the second best product in the world, which is the AirSense 10. And it gives us a chance as we gain regulatory approvals and we scale that production to improve our gross margins there as well. So all those are tailwinds for the gross and net margin of the business as we move through the fiscal year. Hard to predict in that one of the main factors is how do we accelerate in the U.S. and particularly in CPAP, APAP. I will never turn down a patient. If there's demand for a patient and they want a CPAP, APAP, I'm not going to reverse-engineer and we know how to do it. We could reverse-engineer our gross margin up 30, 50 basis points by slowing down sales of product. We're not going to do that. When a patient needs care, we're going to take care of them even if it's a slightly lower gross margin. And by the way, it is really good gross profit dollars, and we get to take that cash flow as you saw really strong cash flow in the quarter and reinvest it in R&D. So we're working on all of the above furiously, and we're going to get success as we go over the next 1, 2, 3 and 4 quarters.

Operator

Next question is coming from Laura Sutcliffe from UBS.

Laura Sutcliffe - *UBS Investment Bank, Research Division - Equity Research Analyst*

I was just wondering if you could talk about how you're positioned to increase your mask supply in the event that the consent decree over at the competition impacts their ability to provide those, for example, if they end up constrained at a facility level?

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

Yes. Look, we have run all sorts of scenario analyses around that. I think one of the differences, if you think in terms of ResMed's ability to work with suppliers in the core device side where in terms of chipsets the whole med tech sector as a group, I serve on the board of AdvanMed and we were advocating for more semiconductor chips for the whole industry. When we were going to Intel and TI and all these companies and sort of begging for semiconductor chips 12, 18 months ago, altogether, we were less than 1% of the supply of chips, and it was very difficult. We did get some. And as you saw, we did have to pay a little more, but we were able to get those contracts with other players and get long-term contracts and get that supply.

In the field of medical-grade silicon rubber, we are one of the top users in the world for this. As you know, we sell tens of millions of mask products per year, and we are an incredibly large part of that supply chain. So if a competitor was not able to sell masks, their demand for that LSR would go down. And those or similar suppliers would then want to keep their factories operating and be looking for other suppliers, and we would be running the game theory and the analysis of where we go and how we go to ramp that production up. So it would be a good problem to have for the business. I think it would be a bad problem to have for patients. But I think the probability of that is relatively low. But if it does happen, we're ready. But Rob, do you have any thoughts on that? Rob Douglas, our President and COO.

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

Yes. Just one other minor comment on that. And we've said this before, because of the relatively low CapEx of our supply chain and the equipment that we need, we generally run with quite a lot of burst capacity if you like and so our ability to rapidly increase volumes as needed is really strong.

Operator

Next question is coming from Sean Laaman from Morgan Stanley.

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

Hope you are well. Mick, I'm wondering if you could characterize for us some of the price dynamics that might have been present during the quarter.

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

Yes. Thanks for the question, Sean. Yes, a simple question, very complex answer. Across the 140 countries and all of the dynamics, I think one thing that I'm comfortable to say though on this is that if you look over the last 4 quarters, our commercial teams have done an incredible job of partnering up with our customers to say, look, inflation is up, costs are up. How do we share some of the pain, if you like, of these increased costs? And we were able to increase some prices on some mask systems and components and some devices where we could. It's tough because customers often don't get much relief from the payers. They did in the Medicare side in the U.S. market, where there was an inflation adjustment up of around 5% January 1, and so that was a benefit for our providers. And so we can share some of the pain there in terms of increased pricing.

But we've also had some surcharges on our products in terms of freight. And although, as I said in the prep remarks, we've seen all the news media that freight costs are all down. Well, yes, okay, they are on a spot price. But 12 months ago or 9 months ago as that works through our inventory, that freight charge is still there and is still impacting our costs, and inflation, although coming down is still high. But I think our commercial teams have done a really good job of partnering up with our customers, walking them through the situation, the reality that costs are up, inflation is up, freight is up, inventory costs are up. We need to work on appropriate pricing to make that happen. And we've had some appreciation in average selling price over these last 12 months. And we'll look to do -- over the next 12 months -- to do an appropriate pricing with customers on a per customer per contract basis to sort of share some of the pain of the increased costs that our industry is having.

But at the same time, we're laser-focused on driving that growth. And so it's a really strong sort of price elasticity question of how do we make sure we get that balance right. But it's a competitive game. Some of our competitors are out there saying the same thing publicly that costs are up, and so we need to move prices appropriately, and we're out there working with customers to make sure that we, as an industry, take care of patients in a sustainable economic way. And that involves both quantity, price and supply over the long term.

Operator

Next question is coming from Lyanne Harrison from Bank of America.

Lyanne Harrison - *BofA Securities, Research Division - VP in Global Equity Research*

Can I ask a question about outlook. So through the early quarters, you mentioned that we were going to see sequential revenue growth through 2023, and we have seen that and that's been fabulous. But with your key competitor out of the market, do you still expect to grow revenue sequentially into first quarter, second quarter '24 or for however long as they remain out of the market?

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

Yes. So great question, Lyanne. Yes, 12 months ago, when it was pretty clear that we had a strong runway there on the devices side. And we -- it was really, we were constrained by our own production. I was able to very strongly say, look, I am confident that our supply chain team has got access to this reengineering, redesign and redeployment of key components, particularly electronic components, particularly semiconductors, and we did that. And we grew device revenue every quarter throughout fiscal year 2023, as you noted. And I was really excited with the team on that.

As we look forward to fiscal year '24, we don't give guidance really on the top line. Brett's given some really solid guidance on our SG&A, our R&D, our effective tax rate and how we're looking in those parts of the business that are very controllable. As I said in some of the earlier questions, we had so many moving factors in overall demand in the market. But look, I'm confident because new patients continue to come into the funnel, right? That's happening across the world. And it's not happening randomly. We're driving demand gen programs. We're driving them in Australia, New Zealand with our Awaken Your Best campaign. We're driving them through our German teams, our India teams, our social media programs, in our China team is really strong social media demand gen. And so we're getting new patients in the funnel.

And there was a glut of patients who couldn't get a replenishment device when the device hit 3 years or 5 years or whatever time their insurance allows or they, as a consumer, decide that they want to get to the next-gen product. And I think the AirSense 11 and all its features, its engagement with the patient with compliance coach, and its ability to engage with them directly on the touchscreen has driven some demand as well. So all that together make me confident that over the fiscal year, we're going to have strong demand.

But as you go from Q4 to Q1, there's a seasonal impact. And Northern European and U.S. markets take summer vacations, and these have impacts seasonally on the business. And so traditionally, Q4 to Q1 isn't a one up. I'm not giving guidance for it, but traditionally that's the way it happens. We're not -- we're no longer supply constrained. We are back to a demand environment. And then there's a factor of that #4 competitor probably not coming back during the next 60 days through so the end of this 90-day period. But I'm not going to jump in and predict on that. All I'm going to say is, we're out there all day every day, driving demand gen of new patients in, we are out there farming for patients who need to get a

replacement device. And every day, we're engaging with patients on myAir and reminding them the importance of a clean hygiene and the new mask and engagement with their digital app. So all of the above gives me very strong confidence for high growth of ResMed throughout the year. But I'm not going to call it on an every 90-day basis here. We just don't do that on the top line.

Operator

Next question is coming from Chris Cooper from Goldman Sachs.

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

So Mick, on AirSense 11, you sort of emphasized its importance for gross margin. You also said at the start of the call, you sort of expect this to remain on allocation for a few more quarters yet. I know this time frame was probably a bit longer than you'd hoped. I just wanted to confirm whether that's entirely a function of supply chain at this point? Or I guess whether there's any sort of strategic consideration to manage volumes during such an unusual competitive dynamic?

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

Yes, Chris, thanks for the question. We've really been focused on that patient and making sure no one is left behind as I said in an earlier question. And although the AirSense 11 is better margin for us, and it's better innovation, and it has a higher engagement on the myAir app, which drives engagement, adherence, mask resupply and everything. Our view is that if there's a patient available and we have the parts and pieces and the ability to make an AirSense 10 and take care of that demand now while we ramp AirSense 11, we're going to do it. And we're going to take care of that patient. By the way, there's some really strong upside for that patient, and that the alternative is a competitor device, which would not be as small, quiet, comfortable and connected. And so they have a much worse experience than the AirSense 10 with a competitive one. So it's better for the patient. It is slightly lower margin for us. But we get that patient on therapy. And there is the better together with ResMed that it's more likely, hopefully, that they get a ResMed mask, and that they use that mask for the rest of their life. And so I think there's an overlap there, if you like, of altruism and the profit motive to do the right thing on a gross profit cash flow-driven environment, and we're not going to manage just to a GM line and say, well, let's not do that and make those products.

And so it's less -- I mean, it's strategic in this way is that our brand is about patient care. Our brand is about taking care of someone who's suffocating and getting them out of the hospital and doing that. And if we have to do it with an AirSense 10, which is an amazing 7-year-old platform, then we're going to do it. If we can do it with the brand-new AirSense 11 platform, we're going to do it. And look, nothing slowing us down. Our quality and regulatory teams are going geography by geography to get the AirSense 11 approved in each of the regulatory environments. So as soon as that is, we can start selling the products. But the ramp up on AirSense 11 is probably not as fast as it would be in a market where you had all 5 major competitors competing there because of that excess demand. We're covering a lot of that with the AirSense 10. So that's sort of how we're thinking about it: patient-centric, patient demand, take care of that patient now, get them on our ecosystem and then ramp as fast as we can, AirSense 11. And we're doing that. Nothing slowing down, the accelerator is firmly pedalled to the floor on AirSense 11. And so everyone we make, we sell, but it will be on allocation just given the huge demand that we see in the market right now, Chris. Thanks for the question.

Operator

Next question is coming from Dan Hurren from MST.

Dan Hurren - *MST Marquee - Healthcare Analyst*

Mick, after third quarter result, you seem to be very confident about gross margin. In fact, I think in the time we know that was our most positive gross margin commentary we've heard out of ResMed in recent memory. So I know you've spoken component costs and why you don't need the gross margins. But what else changed since the time you gave that commentary to the results?

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

Yes. Thanks for the question. And I think actually, if you go back and look, the -- all the factors that I talked about 90 days ago, we're talking about today, but in addition to the AirSense 11 ramp that we're putting together there. What happened in these 90 days that was unpredicted was there was more demand what -- we thought a competitor may be back, and there was more demand for CPAPs and APAPs, and we didn't -- I know the exact number of how we could have slowed down our AirSense 10 generation to get gross margin to be plus 30 basis points from Q-to-Q. But we didn't engineer it and reverse-engineer it that way. We said there's demand out there, let's go take care of those patients. That was the unexpected factor. It was U.S. CPAP and APAP demand. And when you look through the numbers, you'll see that it was incredibly strong on gross profit generation and cash flow generation, incredibly strong during the quarter. And we did think about it. Oh, gosh, do we follow through in saying, "Oh, we want to get accretive GM 90-day to 90-day point? Or do we say take care of that patient?" And we said, no, we're going to do the right thing. We're going to take care of the patients.

So we're thinking about the long-term here. But no, I'm still bullish over this fiscal year for sure. I -- you never can know what demand is going to look like and where it's at. And we are not going to not take care of a patient. But as those higher inventory costs work their way through our system, there's opportunity for gross margin improvement as we go forward. There's also the impact of -- if you looked at the SG&A, this time a year ago, in the June quarter of 2022 versus 2023, there was still a lot of people on that sort of COVID, I'm not traveling, I'm not going to see customers, I'm not going to do the strategic meetings and the planning meetings. We have opened some of that up, as you saw in our SG&A, and so that's impacting our net margin as well. We're going to manage those tightly and carefully. And we'll probably have some further vigilance, if you like, on our SG&A. We won't be pulling back really on R&D. I think that the innovation engine has to continue to grow, and we're doubling down on AI. And I think our leadership in digital health, we have to make that happen.

So I'm still bullish throughout the fiscal year of FY '24, but we're not going to not take care of a patient if there's excess demand with a CPAP and APAP to manage one component of the P&L versus taking care of the patients and thinking about the 1-, 3-, 5-year strategic engagement with the patient, with the physician, with the provider and doing the right thing for the industry. So that's the sort of factors that have changed in the next 90 days. And I hope actually all this comes together, and we continue to do both, right, drive the needs of the patient and be able to get accretion in our GM. And I'm very confident we'll do that over the coming 3, 6, 9, 12 months.

Operator

Next question is coming from David Low from JPMorgan.

David A. Low - JPMorgan Chase & Co, Research Division - Research Analyst

Mick, could I just comment a little on what you saw in the ex-U.S. market. Obviously, last quarter, we saw the big vent sale -- ventilator sale move to China. Just wondering if there's any countries you'd call out or any items we should be aware of, please?

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

Yes, David, that's a good point. We didn't really see anything of material context in this quarter in terms of exacerbation of COVID that led to hospital-based, to life support ventilator sales. And so we're back to, I would say, the sort of steady growth that we see in our neuromuscular disease, our COPD, and other sort of respiratory insufficiency parts of our business for life support vents. On the noninvasive vents and adaptive-servo vents and bilevels, we're back to steady market growth, and, actually, we saw strong double-digit growth as those post-COVID, we're starting to see the clinics open up and patient flows start to come back. Rob, any thoughts on ventilators?

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

No, not on ventilators because just going to comment on masks. The masks in all these other markets were really strong and really showing underlying strength of the market, not affected by recall dynamics or anything like that. So really the whole patient diagnostic systems are working in order, and everything is going strongly.

Operator

Next question is coming from Steven Wheen from Jarden.

Steven David Wheen - Jarden Limited, Research Division - Analyst

I just wanted to ask Brett about the working capital position. Again, last quarter, you were thinking that you'd be able to make some inroads into those, into the inventory balances that you had such that we might see a bit of more of release of cash. But obviously, inventory stepped up again, as has the receivables. Is that just building more to the demand that you see? Or could you just help put that into a bit more context as why it didn't quite play out the way you thought?

Brett A. Sandercock - ResMed Inc. - CFO

Yes. Steve, it's Brett. The inventory actually came down a little bit sequentially. So that's sort of tracking down how we're expecting -- we expect that inventory balance should decline over the course of FY '24 as well. The receivables, you're right, it was up a little bit, but that's really driven by the revenues.

I think overall on the working capital, we're in pretty good shape. It's up a little bit this quarter. But when you look at that, we -- it's really the timing around tax payment this quarter. So we paid higher tax this quarter than we would typically do each quarter. So that's -- that drive, if you like, a little bit of negative working capital. But again, that's just a timing element. So we're expecting pretty robust cash flow generation through each of the quarters in FY '24. And we'll continue to work hard on the working capital, bringing that down. A big driver of that will obviously be the inventory and working that down progressively over the fiscal year.

Operator

Next question is coming from Mike Matson from Needham & Company.

Joseph Scott Conway - Needham & Company, LLC, Research Division - Research Analyst

This is Joseph on for Mike. Could you maybe talk about the new patient and RePAP backlog internationally? I guess the way that I understand it is it fully worked through in the U.S., but there's work to do internationally. I don't know if you -- if that's the case and if you could size that at all?

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

Yes. Look, I don't think we've fully worked through the backlog of patients in the U.S. in terms of patients who want to get -- whose insurance has got to the 5-year point, if they're Medicare or 3, 4, 5, depending on which private payer they're under. And so I do think our competitors' actions slowed down that, particularly if they are on a competitive device and the demand limitation, and the physician is saying, "Look, I've got to take care of new patients. They weren't as prone to write prescriptions or to allocate RePAP if you like, for patients." So I actually think there's some runway still left on RePAP within the U.S. geography. And I think that's even more so in other markets.

As Rob just noted and as we talked about, the engagement with consumers and patients in different geographies is driving mask growth. And any quarter, to have 14% revenue growth in masks in Europe, Asia, rest of the world would be incredible. And that's not driven by any recall dynamics whatsoever from competitors. Everybody's been competing in masks globally. And so I think that speaks to our ability to hopefully have a sustainable approach to RePAP, not only in the U.S., where we have incredibly strong relationships with Brightree and myAir directly to patients directly to providers, but the ecosystems that we're generating in some of our other sort of omni-channel markets around the world. So I think the opportunity for RePAP in the U.S. is still there over this fiscal year and beyond and to make it a rhythm, right? So it becomes a steady part of the growth of the devices and to drive it. I think there's even more opportunity in the other parts of the world, leveraging the work we've done on the mask side to then remind patients and track them when they're at that 3-, 4-, 5-year time period to pull forward. Now I want to be there with the appropriate supplier. So I'm not jumping ahead of ourselves, but we do have the programs and capabilities to do that. But I think the demand is there inherently.

Operator

Our final question today is coming from Saul Hadassin from Barrenjoey Capital.

Saul Hadassin - *Barrenjoey Markets Pty Limited, Research Division - Analyst*

Mick, just wondering on masks. It's been a while since we've seen some new product coming out from ResMed. Just wondering how much has the competitor recall impacted on your ability to continue to focus on new product development and new product launch? And I guess, on the mask side, should we expect anything sort of near-term in terms of a refresh of the mask portfolio?

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

Yes. So it's a great question. And yes, our R&D team have obviously been incredibly focused on the reengineering, the resupply and the redesign on our core platforms, and we're able to do that, right? So we're able to get the supply back of Air 10s as you saw and Air 11s. But yes, look, we had the whole board down in Sydney last quarter, and we were looking through the pipeline of devices and masks. And it's incredible. It's really exciting. I don't like to get ahead of my commercial teams, and one of them is at the table with me now telling me to keep quiet. But I can tell you, I'm very excited about the pipeline. There will be new innovation, new masks from ResMed as we go through this fiscal year. And as a personal user of these products, I try every new mask that comes out. And this new one, which has a great project name that I'm not able to say, but it's a beautiful island that you can travel to by boat. I have tried that mask and it's incredible, and I can't wait for that to come to the market.

But yes, look, we do have masks that are coming in the pipeline that are working their way through regulatory and then, of course, commercial ramp-up to make sure that when we deliver, it's ResMed quality, ResMed capability, first-time fit, incredible adherence and to drive through the channel. And so you'll see those come to our major markets and then globally throughout the fiscal year. So I'm excited about that pipeline.

The one that I can talk about is the digital side where we've launched an AI product, and I'm really excited as those get more traction, we'll talk about how the digital products and the mask products throughout the year are going to impact and keep our incredibly strong double-digit growth that we saw this quarter.

Operator

We reached the end of our question-and-answer session. I'd like to turn the floor back over to Mick for any further closing comments.

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

Yes. Thanks, Kevin, and thanks to all of our stakeholders for joining us this last hour as we talked through our results, and we'll talk to you again in 90 days. In closing, I want to thank the 10,000 ResMedians. Many of you, our shareholders have listened to these calls as well. Thanks for your

dedication and hard work helping people sleep better, breathe better and live better lives in 140 countries. These results are yours, incredible double-digit growth. Thanks for all that you do. I'll hand the call back to you, Amy, to close us out.

Amy Wakeham - ResMed Inc. - Chief Communications & IR Officer

Awesome. Thank you, Mick, and thanks, everyone. We do appreciate your interest and your time. If you have any additional questions, please don't hesitate to reach out directly. This does conclude our ResMed's Fourth Quarter 2023 Conference Call. Kevin, I'll turn it back to you to close the call.

Operator

Thank you. You may now disconnect. We do thank you for your participation today.

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