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# EDITED TRANSCRIPT

RMD.N - Q2 2024 Resmed Inc Earnings Call

EVENT DATE/TIME: JANUARY 24, 2024 / 9:30PM GMT

**OVERVIEW:**

Company Summary





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## PRESENTATION

**Operator**

Hello, and welcome to the ResMed Second Quarter Fiscal Year 2024 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 Chief Investor Relations Officer, Amy Wakeham. Please go ahead, Amy.

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

Great. Thank you, Kevin. Hi, everyone, and welcome to ResMed's Second Quarter Earnings Call for fiscal year 2024. We are live webcasting this call, 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 presentation. Both of these are now available. During today's call, we will discuss several non-GAAP measures that we believe provide useful information for investors. This information is not intended to be considered in isolation or as a substitute for the GAAP financial information. We encourage you to review the supporting schedules in today's earnings press release for a reconciliation of these non-GAAP measures to the GAAP reported numbers.

In addition to our discussion today, it will include forward-looking statements including, but not limited to, expectations about our future financial and operating performance. We make these statements 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'll now turn our call over to ResMed's CEO, Mick Farrell.

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

Thanks, Amy, and thank you to all of our shareholders for joining us today. Our second quarter fiscal year 2024 results reflect strong execution across our entire business, driving double-digit top and bottom line growth. These results are a testament to the incredible efforts of the global ResMed team. Our results were driven by double-digit global growth in both devices and our Software as a Service business, together with high single-digit global growth in our masks and accessories business, holding our leading market share amongst high comps from the same quarter a year ago. In terms of bottom line leverage, our reorganization efforts and efficiency efforts in the quarter have set us on a clear trajectory of profitable growth.

Taking a step back, all 10,000 ResMedians are energized about the opportunities in front of us. There are over 2 billion people worldwide suffering from sleep apnea, chronic obstructive pulmonary disease, respiratory insufficiency due to neuromuscular disease or insomnia. These chronic conditions form a health care epidemic in which ResMed is uniquely positioned to help. We believe that health care should be delivered in the lowest cost, lowest security and highest comfort location possible. Very often, that is a patient's own home.

Our end markets remain underpenetrated with many opportunities to add value, reduce friction, lower costs and improve patient outcomes. We support hundreds of millions of people as they take control of their health care journey and navigate the complex health care world outside the hospital system. ResMed is the global leader in digital health solutions with over 17 billion nights of medical data in the cloud and over 23.5 million 100% cloud connectable medical devices sold into over 140 countries worldwide. We are the clear market leader in sleep apnea, a huge and growing market with over 1 billion people impacted globally.

Our category-leading flow generator platforms grew 11% year-over-year. We have achieved and are maintaining supply of our two 100% connectable AirSense platforms, with unconstrained supply of the AirSense 10 platform globally. Every quarter, we continue to gain regulatory approvals to launch and to increase delivery volumes of the best-in-class AirSense 11 platform on our pathway to support more and more patients worldwide. Our commercial teams are successfully demonstrating the clinical and economic benefits of the ResMed mask portfolio.

During the quarter, our masks and accessories business grew 9% year-over-year in a highly competitive market, maintaining good market share with all players in the field in this category globally. We are excited to have achieved regulatory and reimbursement approval for our latest and greatest mask innovation and we look forward to bringing this technology to market soon. I have personally worn this new mask and our test data show, not just n equals 1 from the CEO, that it is highly favored by physicians, respiratory therapists and especially the most important customer, our patients.

In terms of maintaining our momentum of mask and accessory growth, our clinical and commercial teams continue to partner with physicians and providers to drive resupply programs directly with their patients. Peer-reviewed and published clinical evidence shows that using resupply programs leads to better patient adherence and to better patient outcomes. This is proving out in the real-world customer by customer. We continue to see strong growth in the U.S. mask and accessories business, where resupply programs are powered by our digital health ecosystem, including AirView for physicians, Brightree for home care medical equipment providers and myAir for patients. Outside the U.S., we are focused on developing, launching and scaling our direct outreach and subscription programs, to help consumers take control of their own health and engage directly in refreshing their own mask, their own tubing, their own humidifier and other accessories.

The importance of respiratory health and respiratory hygiene in the eyes of consumers has seen a permanent uptick since 4 years ago when the COVID-19 epidemic started. We're supporting our customers with digital solutions and services to meet their needs and to ensure they have clean and fresh equipment to best treat their sleep suffocation and improve their health. Before I review updates on our key strategic priorities, I'd like to discuss recent actions we have taken to accelerate profitable growth across ResMed and to power our long-term success.

Last quarter, I discussed the steps we've taken to ensure that we can refocus and drive even more profitable growth. We stopped some projects that were not working out and we increased investment in areas that will be pivotal to our long-term success, including our digital health technology investments as well as focused device platform and mask technology development. We have introduced a new operating model centered on making ResMed even more product-led, even more customer-centric and even more brand enhanced. We will measure the success of this new 2030 operating model by an increase in the velocity of new product innovation as well as enhanced value in the ResMed brand while accelerating profitable growth. As the founder of ResMed states, innovation is not just invention of a great new technology is when a customer loves it, adopts

it and chooses to pay for it. We have an incredible legacy and an exciting product pipeline to bring to market. Let's now turn to a discussion of our 3 key strategic priorities.

Number 1 is to grow and differentiate our core sleep health and breathing health business. Number 2 is to design and develop and deliver market-leading med tech and digital health solutions that can be scaled in 140 countries plus worldwide. Number 3 is to create and leverage the world's best software solutions for care delivered outside the hospital and preferably in the home. In terms of addressing strategic priority #1, as the world's clear leader in the field of sleep apnea and breathing health, we're laser-focused in 2024 on ramping up our demand generation initiatives. We're raising awareness and creating pathways for patients to find access to care for sleep suffocation across specific global markets. We are leveraging traditional health care channels and investing in cost-effective social media-driven demand generation campaigns to help consumers who are concerned about their own sleep and breathing to find their way into screening, diagnostic, treatment and management pathways.

Our goal is to provide a digital health care concierge service to help guide people on that journey. We are tracking new patient starts in our physician and provider-based ecosystem, which now contains more than 26 million patient records as well as the new user starts in myAir, which is a patient app where patients choose to participate in their own personalized health care journey to better sleep and better breathing. Our goal is to cost effectively drive more and more of the over 1 billion people worldwide who need our help into the channel. There are 2 megatrends that can have an influence on increasing that patient flow, 1 from big consumer tech and 1 from Big Pharma. Let me talk briefly about each of these megatrends.

Many of the big consumer tech companies are increasing their focus on the area of sleep wellness. Apple has sleep wellness tracking built into its latest-generation Apple Watch and has plans to enhance that capability with further sleep quality assessment. Google's Fitbit division has sleep wellness tracking built into its platform. WHOOP is doing the same. Samsung have not only built sleep wellness tracking into its latest operating platform, but is helping to define sleep personas to help consumers better understand a 30% of their lives they spend in the state of sleep.

We love this attention on the field of sleep wellness and many of these technologies will help each person find out if they have issues with sleep architecture, issues with breathing during sleep, or issues maintaining high quality sleep. This could be one of the biggest waves of people taking control of their own pathway for discovering they have sleep apnea or they have insomnia, or maybe they have both, a state that is called COMISA for comorbid insomnia and sleep apnea. Ultimately, this will lead to increasing patient growth for ResMed overall. And our goal is to best educate the person as they move from sleep wellness tracking to sleep health tracking and from consumer awareness into a true health care pathway for screening, diagnosis, treatment and ongoing management of their chronic condition. ResMed plans to be there with the person through that entire journey.

In terms of the impact of megatrends from big pharma, the current focus is squarely on GLP-1 medications. Let me take some time to address what we are seeing in the market with patients on latest-generation GLP-1 therapies and positive airway pressure therapy. We're tracking a cohort of over 0.5 million patients with prescriptions for both GLP-1 medications and positive airway pressure therapy. These data are included in our investor deck, so you can review them there on our website, but I'll briefly summarize what we have observed. Around 6 months ago, there was a thought among some in the market that patients on GLP-1 medications would be less likely to start positive airway pressure therapy.

We stated at the time and still do, that this was not likely the case as important risk factors such as craniofacial geometry, gender, age and the basic physics and anatomy of the upper airway would remain unchanged despite this new pharmaceutical therapy option. Still, the theory remained. So now we have real-world data and real-world evidence at scale. Our analysis of over 529,000 patients with GLP-1 prescriptions shows that not only is there not a reduction in the propensity to start positive airway pressure therapy, it is the exact opposite.

For patients who have been prescribed a GLP-1, there is an increase of 10% of the absolute percentage of patients that commence positive airway pressure therapy. So as an example, if you take a baseline of 75% of patients that commence PAP therapy after their prescription on average in a certain group, that would become 85% of those same patients who were on a GLP-1 that would commence positive airway pressure therapy. And by the way, the vast, vast majority of these GLP-1s are the latest generation medications. Another hypothesis about 6 months ago was that patients on GLP-1 therapy and PAP therapy would quit their PAP therapy, their CPAP or their APAP at a higher rate than the general population over time. The real world data, again, with a cohort of over 0.5 million patients shows the exact opposite. At t equals 12 months after therapy commencement

on PAP, the delta from general PAP population to a PAP plus GLP-1 prescribed population shows an increase in the resupply rate of 300 basis points.

So again, as an example, if the general population resupply rate at 12 months was, say, 70%, it would then become 73% for the population that was prescribed both PAP and GLP-1 therapy. This delta actually increases over time going further with the delta from the general PAP population receiving resupply at 12 months being 500 basis points higher for a population prescribed both PAP and GLP-1s. Here at ResMed, we believe in treating the whole person, including a combination of what Professor Bill Dement, one of the founders of the field of Sleep Medicine, may he rest in peace, called the Triumvirate of Health. That triumvirate is one, regular cardiovascular exercise; two, balanced diet and nutrition; and three, good sleep and breathing. We believe that addressing all 3 aspects results in the best patient outcomes.

In terms of best-in-class treatments for sleep apnea, achieving that goal of good sleep and good breathing, we have peer-reviewed and published research demonstrating that we can achieve over 87% of patients adherent to our PAP technology by combining our market-leading device platforms with digital health solutions, including AirView for physicians and myAir for patients. Even with this best-in-class global technology, we still have more than 10% of patients that need alternatives. We just can't get them adherent to those 10%. We're investing in these alternative therapies and we are working to help patients who do not adhere to positive airway pressure to find their path to second-tier therapies, such as dental devices where ResMed has invested and scaled the market-leading 3D printed dental device for sleep apnea in Europe called Narval. In addition, we have investments in other third-tier therapies, including pharmaceutical agents with our Apnimed investment as well as hypoglossal nerve stimulation technology with our Nyxoah investment.

ResMed stands for respiratory medicine, not CPAP company, and we want to take care of the patient. We obviously start with the lowest cost, highest efficacy therapies, including CPAP, APAP and bilevel therapies. And we then work through the alternatives to help the person sleep better and breathe better. The bottom line is this, a huge number of people need our sleep apnea treatment solutions today and for the next decade, 2 decades, 3 decades and beyond. We want every patient to find a path to good breathing and good sleep.

Let's pivot for a moment to talk about our digital health technology investments, leveraging the 17 billion nights of deidentified medical data and the 23.5 million 100% cloud connectable devices in our ecosystem. We are investing in several artificial intelligence-driven data products and capabilities in that ecosystem that we call Air Solutions. We're continuing to roll out, one publicly we're talking about, which is called ComplianceCoach to customers in the U.S. market in a controlled market launch. ComplianceCoach is a solution that helps home medical equipment providers to prioritize both digital and personal outreach to improve patient compliance and drive better patient outcomes at a lower cost.

ComplianceCoach models and predicts the likelihood that a particular patient will or will not adhere to therapy based on algorithms built on billions of data points. The AI product then identifies for the HME provider, the key patients who may struggle to meet compliance requirements and takes a step further to drive digital and/or human actions to maximize the probability of adherence across the group. Customers using the product in its initial launch are excited and are starting to see very positive results across their business and for their patients. One final update on AI technology for this quarter. We recently launched an in-market trial of a ResMed developed generative AI product that serves as a digital concierge to help a group of people that we call sleep-concerned consumers, to best navigate as they search for their sleep-related information and they ask questions about their sleep wellness and potential treatment options.

This generative AI tool helps the person identify, engage and enroll on their personal journey to better sleep and better breathing. We're currently beta test marking this product in Asia Pacific, and we will look to scale globally over time. Our goal is to develop and scale this digital sleep concierge so that all those seeking better sleep and better breathing can find their personal pathway for the best outcome, the best treatment and the best long-term care.

Our Respiratory Health business continues to be supported by sustained activity across our noninvasive ventilator platforms as well as our life support ventilator platforms. We continue to invest in clinical and economic trials for high flow therapy that we call HFT to even more cost effectively treat COPD in the home. As we develop these next-generation therapies, we will generate strong clinical evidence and economic outcomes that will support broader adoption of these innovations for treating respiratory conditions at home. The prevalence of respiratory insufficiency due to COPD as well as neuromuscular disease continues to increase, and we offer low-cost, high-quality treatments to help address this health care epidemic.

Turning to our Residential Care Software as a Service business, we had another great quarter with year-over-year growth of 24%. Organic growth of our SaaS business was solid across our Brightree and our MatrixCare brands with another full quarter contribution from our MEDIFOX DAN brand in Germany. Ongoing customer-facing synergies between our Brightree offering in the U.S. and our home medical equipment resupply revenue remains very strong, driving good growth across both our SaaS business and our core sleep health business. We expect to have sustainable organic growth across our portfolio of SaaS solutions in home medical equipment, home health, home nursing and beyond to be in the high single digits as we continue through this fiscal year and to achieve stable double-digit organic growth through fiscal year 2025 and beyond.

We continue to drive operating expense leverage through management of our capabilities for cloud compute, our capabilities for cybersecurity, interoperability and technology development and we plan to accelerate net operating profit growth across our SaaS portfolio and across the entire ResMed business. Our residential care SaaS business remains an integral part of ResMed's growth strategy. This business complements the market-leading software and the market-leading device solutions that we have in our sleep health and breathing health business, and we are well positioned as the leading global strategic provider of SaaS solutions for residential care. We are transforming respiratory medicine and residential care at scale. We are leading the industry in developing, applying and adopting digital health technology across our markets. We continue to scale and drive efficiencies in our operations. We're focused on driving top line revenue growth, focused cost discipline and increased efficiencies to accelerate profitability.

We have created differentiated products and solutions for customers worldwide, driving long-term sustainable value for our shareholders. We lead the industry in digital health technology with the smallest, quietest, most comfortable, most connected and most intelligent solutions, and we don't plan to stop innovating anytime soon. We invest around 7% of our revenues straight back into market-leading research and development. ResMed's mission remains crystal clear: To improve 250 million lives through better residential health care in 2025. This patient-centric mission motivates me and ResMedians every day. During the last 12 months, we have improved over 170 million lives by delivering a medical device directly to a patient or a complete mask system to a patient or a digital health software solution that provides personal care for a patient. We've helped each person to sleep better, to breathe better or to live higher-quality lives with best-in-class health care delivered right where they live. I'm very excited about the opportunities in front of us and the pipeline we have ahead.

In closing, I want to express my sincere gratitude to the more than 10,000 ResMedians for their perseverance, their hard work and dedication today and every day. Thank you.

With that, I'll hand the call over to Brett in Sydney for his remarks, and then we'll open up to Q&A for Brett and me and the team. Over to you, Brett.

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**Brett A. Sandercock** - *ResMed Inc. - CFO*

Great. Thanks, Mick. In my remarks today, I will provide an overview of our results for the second quarter of fiscal year 2024. Unless noted, all comparisons are to the prior year quarter and in constant currency terms, where applicable. We had strong financial performance in Q2. Group revenue for the December quarter was $1.16 billion, a 12% headline increase and 11% in constant currency terms. Revenue growth reflects the ongoing combined availability of AirSense 10 and AirSense 11 sleep devices to support solid underlying global demand and continued growth across our mask portfolio. Year-over-year movements in foreign currencies positively impacted revenue by approximately $11 million in the December quarter.

Looking at our geographic revenue distribution and excluding revenue from our Software as a Service business, sales in U.S., Canada and Latin America countries increased by 9%. Sales in Europe, Asia and other markets increased by 12%. Globally, device sales increased by 11%, while masks and other sales increased by 9%. Breaking it down by regional areas, device sales in the U.S., Canada and Latin America increased by 7%, masks and other sales increased by 10%, reflecting growth in resupply and new patient setups. In Europe, Asia and other markets, device sales increased by 16%, again, reflecting strong demand and significantly improved availability of cloud connected devices. Mask and other sales increased by 4%, reflecting the impact of a strong prior year comparable growth rate. Software as a Service revenue increased by 24% in the December 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 10% in the December quarter.

MEDIFOX DAN contributed revenue of $28 million in the December quarter, consistent with our expectations at the time of the acquisition. Note as we have now passed the first year anniversary of our MEDIFOX DAN acquisition, our future SaaS revenue year-over-year will reflect organic growth. During the rest of my commentary today, I will be referring to non-GAAP numbers. We have provided a full reconciliation of the non-GAAP to GAAP numbers in our second quarter earnings press release. Gross margin increased by 10 basis points to 56.9% in the December quarter. The increase primarily reflects a decrease in freight costs and increase in average selling prices and favorable foreign currency movements.

The benefits are partially offset by unfavorable product mix. Sequential gross margin increased by 90 basis points, primarily driven by a reduction in freight costs and an increase in average selling prices for our devices, partially offset by unfavorable product mix. We remain confident of a positive gross margin trajectory. Like many companies, we are monitoring potential headwinds that could arise in the Middle East conflict. Disruptions in the Red Sea will likely increase sea freight costs and shipping lead times. We're closely tracking the situation and taking action to mitigate potential impacts where we can.

Moving on to operating expenses. SG&A expenses for the second quarter increased by 4%. The increase was predominantly attributable to increases in employee-related costs. SG&A expenses as a percentage of revenue improved to 19.1% compared to 20.5% in the prior year period and reflects savings and cost discipline following specific actions taken early in the December quarter. Looking forward and subject to currency movements, we expect SG&A expenses as a percentage of revenue to be in the range of 18% to 20% for the second half of fiscal year 2024. This guidance reflects the impact of our restructuring activities that resulted in a reduction in our workforce of approximately 5% during the quarter. R&D expenses for the quarter increased by 6%. R&D expenses as a percentage of revenue was 6.4% compared to the 6.8% in the prior year period.

Looking forward and subject to currency movements, we expect R&D expenses as a percentage of revenue to be in the range of 6% to 7% for the second half of fiscal year 2024. Operating profit for the quarter increased by 20%, underpinned by strong revenue growth and modest growth in our operating expenses. Following the acquisition of MEDIFOX DAN, our net interest expense for the quarter was $14 million. And as we continue to pay down debt, we expect interest expense to be in the range of $10 million to $12 million per quarter in the second half of fiscal year 2024. Our effective tax rate for the December quarter was 20.7% compared to 18.3% in the prior year quarter. The increase in our effective tax rate was primarily due to a significant reduction in the tax benefit associated with employee equity compensation this quarter compared to the prior year quarter.

We continue to estimate our effective tax rate for fiscal year '24 will be in the range of 19% to 21%. Our net income for the December quarter increased by 13% and non-GAAP diluted earnings per share also increased by 13%. During the quarter, we recorded $64.2 million of restructuring-related charges following an evaluation of our existing operations and actions undertaken to improve operational efficiency and increase profitability. Restructuring charges included $28.6 million of employee severance and other onetime termination benefits, $33.2 million of intangible asset impairments associated with the wind down of certain business activities and $2.4 million of other asset impairments. The restructure charge has been treated as a non-GAAP item in our Q2 financial results.

During the quarter, we also recorded a provision of $6.4 million for expected costs associated with the recently announced Masks with Magnets field safety notification. This expense has been treated as a non-GAAP item in our Q2 financial results. Cash flow from operations for the quarter was $273 million, reflecting solid underlying earnings and relatively stable working capital balances. Capital expenditure for the quarter was $23 million. Depreciation and amortization for the quarter totaled $45 million. We ended the second quarter with a cash balance of $210 million. On December 31, we have $1.2 billion in gross debt and $1 billion in net debt. During the quarter, we reduced our debt by $130 million. On December 31, we had approximately $955 million available for drawdown under our revolver facility, and we continue to maintain a solid liquidity position.

Today, our Board of Directors declared a quarterly dividend of $0.48 per share. As we advised last quarter, as part of our capital management activities, we resumed our previously authorized share buyback program in the December quarter. We purchased 335,000 shares for consideration of $50 million. We intend to continue to purchase approximately $50 million per quarter in the second half of fiscal year 2024. This will more than offset any dilution from the vesting of equity to employees during the year. Going forward, we plan to continue to reinvest in growth through R&D, pay down outstanding debt and deploy further capital for tuck-in acquisitions.

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

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

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

## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions) Our first question is coming from Margaret Andrew from William Blair. (Operator Instructions)

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

I wanted to maybe follow up on your comments on GLP-1, even more so than the quarter. And I look at that 10% greater likelihood of folks starting CPAP when you're on a GLP, it seems like it could have a pretty meaningful impact for growth. And again, I'm looking at it to say, if you're going from 75% patient new starts in a given period to 85%, that's a 13% bigger market every year. So I guess conceptually, is that something that you agree with? Would it have a greater or less benefit impact if that trend continues? And I guess any comments on a real impact on this over the next 3 years as GLP adoption grows.

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

Yes, Margaret. Look, it's a great question. And as a biomedical engineer, I look at this, and I don't know causality, I just know the correlation. And so we've now got data, the 529,000 data points that show that there's a 10% higher propensity to start PAP therapy if you prescribe the GLP-1 before and then you get the PAP therapy, 10 absolute percentage points higher of the cohort will start PAP therapy. My thought is that this is a more motivated patient, a more engaged patient in the health care system, and they've been brought in by this new therapeutic tool. And so I do think that it will lead to greater growth. This megatrend of GLP-1s will lead to greater growth of patients coming into our treatment pool over time. And certainly, the data is showing that with that cohort of patients.

Yes, your quick math there of an increase, I think, is that if there's full penetration across the whole patient cohort and full adoption GLP-1s across every patient coming through. Of course, that's the maximum state. But I think realistically, as we see this pretty fast rollout of this new pharmaceutical class, we will start to see more patients come into the health care system. Everyone is seeing that across med tech and across health care. They are more engaged and they do seem to be getting prescriptions for many different chronic diseases, sleep apnea is non-exception. And we've got probably one of the highest number of patients in that cohort of over 0.5 million patients that we're tracking. And of course, we've got 26 million patients in our database. So this is a minority of patients that we're seeing on these, but it is interesting within that cohort to see a higher participation rate. Look, our goal will be to leverage that megatrend and to make sure that ResMed is there with the best tools for screening, diagnosis, treatment and management. And we've done that over decades, and we plan to do it ahead.

I think maybe the consumer -- big tech -- trend of sleep wellness tracking might be slightly higher in its impact over time, maybe not as quick adoption, but these sleep wellness tools coming across all consumer tech applications is incredibly exciting. ResMed's goal is there to leverage this demand gen that's coming to us from big pharma and big consumer tech, but then more importantly, to get that personalized health journey so that ResMed can be truly the concierge for that person if they find their path to better sleep and better health. So we do expect these trends to be positive. They won't be immediate. And our job is to drive it over time.

**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 good quarter here. Maybe Mick, I will stay on GLP-1s, we're getting a lot of attention turning toward the Eli Lilly SURMOUNT-OSA study. And maybe the KPIs that you're looking for in that study how relevant do you think the primary endpoint is? Are there other secondary endpoints that are more important? And do you think over time you can collaborate with Lilly to drive the effort of using CPAP with the GLP-1.

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

Yes. Thanks for the question, Anthony. And it's a really pertinent one. Certainly, we're watching the SURMOUNT-OSA trial. It's a pretty small trial. It's less than 500 patients, 500, 600 patients, I believe. So it's not sort of the order of the real world event, real-world data that we have, like 500,000 patients we're talking about there. But I think it will be very interesting to see the presumption is given it's the same biochemical compound as in other trials used for diabetes treatment and weight loss that it will have somewhere in the order of 10%, 20%, maybe even 30% weight loss reduction in this cohort. So that's a metric that's sort of well-known from prior studies. The best evidence from the primary investigator on this Professor Atul Malhotra from University of California, San Diego. His assessment is that, that should lead to pretty significant AHI reductions in the treatment cohort versus placebo, maybe in the order of 50% to 60%, maybe 65% AHI reductions in the cohort of these quite high BMI and quite high AHI patients.

If you listen to a great podcast between Professor Malhotra and Dr. Carlos Nunez, our Chief Medical Officer, which are available on our website. When you've got to spare 45 minutes, but there are some cliff notes that I think are worth sharing here in this investor call is that Professor Malhotra was asked what's the best therapy to treat sleep apnea. Is it, a, weight loss? Or is it b, CPAP. And he said, "Well, that's a false dichotomy, this question, it's a false competition. It's a plus b. It has been for decades and will be for decades in the future. And as a PI on that study, he says, look, we have a new pharmaceutical agent that's going to help with treatment a.

And of course, that will be used in combination with treatment b. So the PI on the study is saying that he thinks the combination treatment of a weight loss medication similar to prior work and bariatric surgery that had much higher weight loss numbers or diet and exercise that had all the variance that we've seen over decades of different methodologies there. But this one does seem to be a good agent for treatment a. And then will need to be combined with treatment b to fully treat the sleep suffocation that the patients will have. So don't trust me, the CEO of the company that makes the therapeutic, trust the primary investigator that's saying, combination treatment has worked for decades and will work for decades. I would expect that to be the outcome the trial.

And in terms of working with big pharma on this, I think they're very focused on other areas like obesity and diabetes, but as much as we can get their attention to talk about sleep and sleep health and to do their D2P advertising to talk about the importance of sleep and sleep health. I think combined with the Apples and the Samsungs and the Googles of the world talking about it, it will be a huge positive for of us in the sleep apnea treatment industry. Thanks for the question, Anthony.

**Operator**

Our next question is coming from Mike Matson from Needham & Company.

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

I guess I'll just ask one on Philips. So I think they've talked about relaunching their flow generators in some of the OUS markets, just curious what you're seeing there? Have you seen that happening? And have they been able to recapture share anywhere?

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

Yes. Thanks for the question, Mike. And yes, certainly in tens of countries in Europe and Asia, we are in full competition with all the global players, including the company you mentioned and the large regionals from Europe and from Asia and have been for many quarters. So they've come back in masks and devices across tens of countries in Europe and Asia. And their goal there when they come back, if they've been out for a year or 2, depending on the time they're out of each market is to fight their way from the bottom. They've got 0% new patient start share when they first come back in and they're trying to fight their way up. And in general, they've had to fight against the #2, the #3 and the #4 player who don't have like ResMed has the leading technology, the best AirSense platform, right? The AirSense 11 globally is the best platform in all 140 countries. The second best platform in, I would say, all 140 countries is the AirSense 10 platform.

So their goal is to then fight against regional player from Europe with the #3 or a regional player from Asia, with the #4 in the countries that they're coming back. And so we're seeing that country by country. We're seeing them fight for that share at the low end. It's our focus as the market leader is on growing the market. And I think they're a fair competitor. We've competed against them for decades since they bought Respironics.

And in general, we've won and taken share. We were winning and taking share from them in 2019. We're winning and taking share from them in 2023 and 2024 as they come back country by country. And if and when they come back to the U.S. marketing devices, by the way, they're already here on masks, never left, and we've been competing and leading them there. I look forward to them coming back to this U.S. market so we can get any stock overhang away about what's it going to look like and what it's going to look like is what it looks like in all the other tens of countries where they fight for share from the bottom and work their way up. And I look forward to competition, a healthy competition. And we seem to do very well in it because we've got the smallest, quietest, most comfortable, most connected and most intelligent solutions, and it's really about that. It's about the value you provide getting that patient to the right care, lowering the cost and improving adherence. And we've done a great job, and I like all global competition in the space.

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**Operator**

Your next question is coming from Suraj Kalia from Oppenheimer.

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

Mick, can you hear me all right?

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

Got you loud and clear, Suraj.

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

Congrats on the nice quarter. So Mick, in the 2030 operating model, right? If I got your commentary right, ResMed brand and profitability, velocity of product control, some of these things that you highlighted, I guess, where does compliance coach fit within the 2030 strategic model. More specifically, I'm just trying to understand how do you measure the ROI in the ComplianceCoach. And I presume this is going to be a primarily a reactive AI model. Any additional clarity would be great.

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

Well, thanks, Suraj. I could spend the rest of the time answering that call around the 2030 operating model. I'll just briefly talk about it and then talk specifically about compliance coach. Our 2030 operating model, yes, it's the 3 tenants, right? The 3 tenants are product-led, customer-centric, brand enhanced. ResMed has always been product-led, but now we have a Global Chief Product Officer, whose sole role is to curate that product

portfolio with an amazing team of hundreds of engineers and marketeers to bring the great innovation to market. So we'll measure the success on that on product velocity, how quickly do we bring innovation to market, time to market, time to success.

Customer-centric. We've always been customer-centric. But we haven't always done the best of analyzing the Net Promoter Scores of patients, Net Promoter Scores of physicians, home care providers, physician payer providers and so on. So really understanding the marketing metrics around that, and having our first Chief Marketing Officer sit at the top table and really be laser-focused on those NPS scores and driving them up and really valuing the multibillion-dollar ResMed brand and enhancing that over time.

And the third part around focusing on profitable growth and driving that leverage with our first Chief Revenue Officer, it's really around that profitable growth.

And if the title was used broadly, I would call it the Chief Profitable Growth Officer rather than Chief Revenue Officer, but really, it's around keeping that discipline on the great growth we've had on the top line, but ensuring we get that leverage through OpEx, R&D and particularly on SG&A in the new world to do things differently with tech.

And that segues into the second part of your question, ComplianceCoach. Yes, Look, this is a great AI tool. By the way, it's not generative AI ComplianceCoach. The other one that we launched in Asia Pacific, the digital concierge is generative AI and has that extra capability. ComplianceCoach is garden variety, what would have been called machine learning is now artificial intelligence, it's a great algorithm, and it's out there. The measure of that one, success on that one, Suraj, is does it lower the cost to serve at that HME or with the same labor force of respiratory therapists and pulmonary doctors can they serve more patients.

So lower cost, higher efficiency, and really, the key metric is what's the adherence rate at day 90, day 365, year 2, year 3, in that patient cohort that's gone through compliance couch. Is it statistically and significantly higher than what that customer was getting before. If they're a best-in-class ResMed customer getting 87% adherence at day 90, does it go up to 90, does it go up to 92. And by the way, those customers are very sophisticated in understanding what that means for their business, what it means for them showing the payers that they reduce costs in hospital care and that they improve outcomes for the patient in how they feel and of course, how they improve their own revenue and hours through replenishment supplies. Anyway, that's my -- the briefest answer I could do to that great question. Thanks, Suraj.

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**Operator**

Next question is coming from Steve Wheen from Jarden.

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**Steven David Wheen** - *Jarden Limited, Research Division - Analyst*

Yes. Just a question for Brett. Brett, I'm just wondering if we could look into the gross margin a little bit further and trying to understand, are we seeing in -- across that quarter, the full benefit of the price that you've taken? Or is that some annualization effect as some customers perhaps roll off contracts and whether or not from a rate perspective, could you just kind of reiterate what your expectations are there, what you're seeing with regard to the pricing following the conflict?

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**Brett A. Sandercock** - *ResMed Inc. - CFO*

Yes. Sure, Steve. So yes, I mean, on the gross margin and recent price increases we put through during the quarter, some of those were obviously the contractual arrangements there as well. So we've put some -- some of it's gone through as a general increase, and then there will be specific contractual arrangements that means those pricing will be a little bit progressive. I guess if you look over the back half of fiscal '24 on that. So let's call that kind of progressively roll through. But we're definitely seeing some of that impact already on that. I think the second part of your question was around -- is that around the sort of freight Red Sea disruptions and so on.

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**Steven David Wheen** - *Jarden Limited, Research Division - Analyst*

Yes. Yes. Just what you were sort of implementing, if you could just repeat that commentary, what you're seeing in the market and how you actually are trying to anticipate or protect yourselves against that.

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**Brett A. Sandercock** - *ResMed Inc. - CFO*

Yes. Yes. So we're definitely seeing the impact there and a lot of that shipping is obviously not going through the Red Sea, but then going around and it's good hope. So that's happening certainly increased lead times, I think, probably you could be looking at 2 to 3 weeks on that. Particularly, this is a particularly freighting to Europe in particular, but also to some extent, to the U.S. where you've got to find alternate freight pass, if you like. So that's having an impact. And we're also seeing some increase in actual freight rates as well. And I think this is an industry wide and not just ourselves. So we're looking at that closely. We're looking at alternative routes. We're looking at multimodal distribution there. So there's a number of things we're looking at to mitigate that where we can. But it realistically probably see some uptick in freight across. It would not manifest in our P&L in Q3, but there could be some headwinds in Q4 on that. But again, we -- I think we've just got to see how that evolves over the next little while.

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**Operator**

Next question is coming from Saul Hadassin from Barrenjoey Capital.

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

Just another question for Brett. Brett, just regarding the restructuring charges and also the charge for the Mask recall. Is that done now in terms of those P&L costs? Or do you expect any further costs to be incurred in third quarter or in fourth quarter this fiscal year.

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**Brett A. Sandercock** - *ResMed Inc. - CFO*

Yes, well, let me through that. I mean, I can't -- I don't think you can rule out restructures from time to time, but I think the material restructure that we did is behind us now. So going -- anything going forward, I think, would be pretty minor on that. So I would say -- I'd characterize that as saying, yes, we've done the big restructure, and that should clear us now for the next quarter.

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

Just to jump in there, Brett, a little bit specifically to Saul's question about the mass with magnets upgrade of our labeling, which was classed as a recall in the U.S. and some other jurisdictions. That cost was fully taken account of in this quarter. We're not expecting to add anything more on the Mask with Magnets action relabel and recall in certain jurisdictions.

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**Brett A. Sandercock** - *ResMed Inc. - CFO*

Yes, absolutely.

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**Operator**

Next question is coming from Mathieu Chevrier from Citi.

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**Mathieu Chevrier** - *Citigroup Inc., Research Division - Assistant VP & Senior Associate*

Simple one, when do you expect to be fully transitioned the AirSense 11 platform.

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

Matthew, a very simple question, but rather complex answer in that we sell in 140 countries worldwide, and each of them -- most of them have their own regulatory pathway and often very different and complex and obviously, labeling language customization of the product for all regulatory requirements needed in all those 140 countries. So we clearly launched in our top countries, we launched in the U.S., many countries in Europe. We just got Japan last quarter, the quarter before and we're starting to ramp up there. And you saw that in the good growth numbers in devices in Europe, Asia and other in the quarter of 16%. There was some good sort of starting that ramp there in a place like Japan, which, as you know, is a fleet driven market versus a by-quarter driven market. And so great to see Japan -- the citizens of Japan to be able to get access to the best in the world technology in the AirSense 11.

But look, we've got hundreds of countries -- over 100 countries, we still have to go there. And so we've got to get regulatory country by country. And we care about people suffocating in all of those 140 countries in the same way. And so our regulatory and quality team with Dawn Haake, our Chief Quality and Regulatory as are working intensely with all the regulatory authorities in those countries and we have to ramp that up. And then in addition, we're ramping up supply. The good news is that we have the second best platform in the world in the AirSense 10, and that is completely unconstrained.

So if you do suffocate and get a prescription in the country that AirSense 11 is not cleared yet, you can get access to incredibly small, quiet and efficacious therapy in the AirSense 10 platform and our best in the world mask platform. And so there's no simple answer to when it will be completely done in 100% in all countries because I think as indifferent to maybe the AirSense 7 to AirSense 8, AirSense 8 to AirSense 9 and AirSense 9 to AirSense 10 generations is that we have a pretty unique citizen situation with our global citizenship here that we are the global leader, and we've got a different responsibility to maintain our second best platform, which is the second best in the world for a little longer.

And so that will be out. And I'm not going to give a defined end date now, but I will tell you this, we're going country by country, we're driving regulatory and we're scaling manufacturing as fast as we can on AirSense 11 because it is better technology, is low cost to make, and we are able to have a premium for it in pricing. So it makes sense for us, the customers and for our shareholders.

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**Operator**

Next question today is coming from Matt Taylor from Jefferies.

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**Matthew Charles Taylor** - *Jefferies LLC, Research Division - Equity Analyst*

I wanted to ask a follow-up question on the SURMOUNT study. I think you outlined a lot of the high-level stuff there really well. My question is a little more specific. I wanted to ask about what you thought you could see in terms of comparing the 2 arms of GLP-1 versus CPAP plus GLP-1? Do you think you'll see a difference there? And what would you make of their results if there is a difference some way or the other?

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

Yes. Thanks for the question, Matt. And so for those of you who haven't read through the nih.gov, feel free to go. But my reading -- I'm a visual learner. There's a split chart that the top half of it on the trial is a GLP-1 side and the bottom half is a placebo side. And so they have this 600-odd or less than 600 patients split between those 2 in a certain proportion. And then within the GLP-1 arm, they split to those on CPAP and those not on CPAP and the same within the placebo. So there ends up being 4 arms if you look at it. But if you go to the end of it, there's an arm that's placebo, no CPAP. So I'd just call that the placebo plus placebo arm.

And then there's placebo plus CPAP arm and then there's GLP alone arm and GLP plus PAP arm. So you start to get down to the subanalyses, it gets less powered. I actually -- I'm reading what you are on nih.gov. And so my presumption is at the highest level, they want to show that a GLP-1 is better than placebo for lowering weight and improving AHI. I think they'll achieve that primary outcome. I mean all the data show that there's 10%, 20%, 30% weight loss reduction and that should correlate to significant AHI reduction. So I think they'll show that. As opposed to then the sub-studies of CPAP versus no CPAP within each of those, look, we've got 35 years of history knowing that CPAP doesn't half treat, right? I mean, the best that I've seen from weight loss reductions in bariatric surgeries and the best on the GLP-1 prelim data is that it can half treat, right? Maybe 50% reduction in AHI. I'd call that half treatment. I don't think any pulmonary physician in the world would be happy with half treating an AHI with positive airway pressure.

Frankly, if you're not turning the AHI to less than 5, you're not truly treating the patient. And if it's higher than 5, it might be residual central and you have to move them to a bilevel or it might be complex sleep apnea, you have to move them to adaptive server ventilation. So there's so many options between CPAP, APAP bilevel ASV that the physicians should walk through, but they wouldn't be happy unless the AHI is less than 5%. I think the probability -- and don't trust me and my quote on this, Matt. Again, the primary investigator on the study, Professor Malhotra said, the idea that weight loss alone can treat sleep apnea is preposterous. That was the word he used.

So you can use -- and he's the PI on the study. You can use his thoughts to what he thinks between the PAP arm and the non-PAP arm. So he's sort of leaning towards what he said earlier, that best treatment for sleep apnea is not: a, weight loss or b, CPAP, it's a plus b. And so that's what I expect this study to show. And we'll see the data. They will be out there and release whatever they want to release in headline and we'll continue to go. We'll continue to grow. We'll continue to drive patients into the funnel, and I think this therapeutic class will help us over the coming decade to bring more patients into the funnel.

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**Operator**

Our next question today is coming from Lyanne Harrison from Bank of America.

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

So Mick, Brett and Amy, I might ask a question about your device and mass sales there. So obviously, strong device sales, your resupply programs, obviously, giving that some focus. But masks this quarter came out weaker than where we expected. Can you talk us through where the disconnect there might be?

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

Thanks for the question, Lyanne. And yes, really, really happy to take questions and talk about our devices business and our mask business. So look, devices growth globally, incredibly strong in the quarter at 11%. Masks growth globally incredibly strong at 9%. We talk about the market being mid-single-digit growth for devices, so we are clearly well ahead of that with the launch of AirSense 11 in Japan and Europe, Asia, Rest of World and doing well in the U.S. a couple of hundred basis points above.

And then in masks and accessories, you talked about global growth being in high single digits. And so beating that in U.S., Canada, Latin America, but what you're probably focusing on is the Europe, Asia and Rest of World growth there in Q2 FY '24 being 4%, right? And just to be clear, the Q2 FY 2023 growth in that same category was 14%. And we were taking 500 basis points a share 12 months ago and then losing it this quarter. I really think if you look at the weighted average over that, which is, what, 18 divided by 2 is 9% is sort of more in line with the market growth in that mid- to high single-digit growth of masks there. And look, there's some things around some contracts with the particular countries that were moved from December to January and others. I'm not going to go to all the details other than to say, we look really closely at share.

We look really closely at what we're doing. And this 90-day snapshot 4 quarters ago, which showed 14%, we weren't taking 500 basis points a share. We were holding share and growing in a little -- a category here or there. And now this quarter at 4%, we're not losing 500 bps a share. We're actually holding share across that and it's due to some of those shipping areas, launch areas and frankly, a couple of tenders that will move from one month

to another. So really not much to see in that. But what I will say is that as we move forward, maintaining that high single-digit growth in devices globally, and the high -- sorry, mid-single-digit growth in devices globally and high single-digit growth in masks globally is not a given. We've got to drive that demand. We've got to leverage this big pharma trend. We've got to leverage the big tech trend, and we've got to get better at doing demand generation in the areas where we know we can push it up. And so that's what we're going to be focused on going forward. I hope that answers your question, Lyanne.

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**Operator**

Our final question today is coming from Michael Polark from Wolfe Research.

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**Michael K. Polark** - *Wolfe Research, LLC - Director & Senior Analyst*

I will ask a mask question as well following up there in a slightly different way. So the U.S. number was up 2% sequentially. Normally, you see a high single-digit increase Q-over-Q kind of year-end seasonality in the U.S. deductible flush, that kind of thing. Kind of what are the puts and takes in that number? And the specific question is, did the Magnet field safety notice kind of limit your ability to fully capture mass demand in the quarter? Or were there other influences?

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

Yes. Great question, Michael. So yes, U.S., Canada and Latin America, a 10% growth in the mask in the quarter. It was actually a very strong market growth rate, high single digits, holding share there. We do see that December, particularly for U.S. markets where high deductibles and deductibles reset December 31, some good revenue there. And so we had good comp from the year before, and both solid numbers there from the comp year before this 10% U.S., Canada, Latin America growth. So I think we did really well there as we closed out the quarter. In terms of any impact from the Masks with Magnets update on our labeling class in the U.S. by the U.S. FDA as a recall, I got to tell you, there was no product removed from the market. This was about having our plastic clips as an option, which we scaled up manufacturing and have them as an option.

So when a patient is set up, if they're a very, very small minority of people who haven't implanted pacemaker or other metal device in their upper chest or craniofacial area, then those patients are offered an upgrade to the plastic clips. For everyone else, the other 95%, 99% of patients they keep the convenience of the magnet. So that if they go to the bathroom in the night, they can come back in the dark and just clip it on and not have to seek for plastic clips to clip together the magnet completely goes on there.

And so as we've done that labeling upgrade, and we had a competitor do this similar one about 12 months ago, the market has been very trained in knowing to ask questions about implants, to ask questions about our partner's implants. And if they have that to offer the plastics clips, which are fully available on ResMed masks as an alternative to our Mask with Magnets. The Masks with Magnets are so convenient. They're doing so well and for 99% of people, they're great. For that 1%, the HMEs are very comfortable now to ask those questions. And the other 140 countries we are working through the appropriate ways to ask the questions and get people the best mask and have the best fit and drive the best adherence over time. But they had no impact on the quarterly sales whatsoever. And we don't expect an impact going forward because this was an upgrade to a labeling that was actually in line with clinical practice over the last 12 months. And it just makes sense to do that. Thanks a lot for the question, Michael.

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**Operator**

We've 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.

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

Thanks, Kevin, and thank you again to all of our stakeholders for joining us on this call. The opportunity in front of us is huge and largely untapped. It's an incredible runway. We see more and more people coming into the health care system, and this will benefit us as we seek to help them sleep better, breathe better and live better lives in 140 countries. Thank you to all 10,000 ResMedians. Many of you are also shareholders, for what you do today and every day. With that, I'll hand the call back to Amy to close this out.

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

Great. Thank you, Mick. Thanks, everyone, for listening. We do appreciate your time and your interest. If you have any additional questions, please don't hesitate to reach out directly. This does conclude our second quarter 2024 conference call. Kevin, you can go ahead and close this out.

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**Operator**

Thank you. That does conclude today's teleconference and webcast. You may disconnect your line at this time, and have a wonderful day. We thank you for your participation today.

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