2Q19 Earnings Call

Good afternoon and welcome to the Omnicell second quarter 2019 earnings call. Joining me today is Randall Lipps, Omnicell Founder, Chairman, President, and CEO.

This call will include forward-looking statements subject to risks, uncertainties and other factors that could cause actual results to differ materially from those expressed or implied. For a more detailed description of the risks that impact these forward-looking statements, please refer to the information in our press release today, in the Omnicell annual report on Form 10-K filed with the SEC on February 27, 2019, and in other more recent reports filed with the SEC. Please be aware that you should not place undue reliance on any forward-looking statements made today.

The date of this conference call is July 25th, 2019, and all forward-looking statements made on this call are based on the beliefs of Omnicell as of this date only. Future events or simply the passage of time may cause these beliefs to change. Finally, this conference call is the property of Omnicell, Inc., and any taping, other duplication or rebroadcast without the express written consent of Omnicell is prohibited.

Randall will provide an update on our business. After Randall's remarks, I will cover our results for the second quarter of 2019 and our guidance for the remainder of the year. Our second quarter financial results are included in our earnings announcement which was released earlier today and is posted in the "Investor Relations" section of our website at omnicell.com. Our prepared remarks will also be posted in this same section.

Let me now turn over the call to Randall.

Good afternoon! We are pleased to share the results of another strong quarter as the healthcare industry continues to recognize the importance of the vision of the Autonomous Pharmacy. As we've discussed previously, this vision of creating a zero-error, fully automated and digitized infrastructure will lead to enhanced safety, control and efficiency of medication management across the continuum of care. We have made significant strides this quarter to advance this vision and engage customers to join us on this journey.

Our business is very healthy and continues to grow profitably.
Key financial results from the quarter include:

1. Record revenue of $217 million up 15% from the same quarter of 2018
2. Non-GAAP EPS of $0.67 per share, compared to $0.46 per share in the same period last year, representing a 46% increase.
3. Our product backlog at June 30, 2019 is at an all-time high and is growing faster than our product revenue.

During this quarter, we continued to see strong momentum of new customer partnerships that are embracing the vision for the Autonomous Pharmacy. The Autonomous Pharmacy integrates a comprehensive set of solutions, powered by the Omnicell cloud data platform, across three key areas: 1. Automation solutions designed to digitize and streamline workflows; 2. Intelligence that provides actionable insights to better understand medication usage and improve pharmacy supply chain management; and 3. Automation of medication dispensing workflows, which includes expert services that serve as an extension of pharmacy operations to support improved efficiency, regulatory compliance and patient outcomes.

Some of our recent partnerships include:

<u>Spartanburg Regional Healthcare System</u>, an integrated healthcare delivery network in South Carolina and North Carolina, has selected Omnicell solutions at their flagship research and teaching hospital, Spartanburg Medical Center, as well as the newly acquired Mary Black campuses. Spartanburg, like many provider networks, is building a Centralized Distribution Center (CDC) as the main hub for pharmacy supply chain management. Central to operations in this new center will be Omnicell's XR2 Automated Central Pharmacy System, a robotic system

designed to automate critical workflows to maximize inventory control, help improve efficiency and increase medication safety. Spartanburg will also have the ability to better utilize health data analytics through Omnicell Performance Center.

MUSC Health, named the number one health system in South Carolina by *U.S. News and World Report*, will be implementing Omnicell's Robotic IV Insourcing Solution (RIIS) to bring sterile compounding in-house as part of the health system's Central Pharmacy operations. This unique program combines advanced robotic technology, data and expertly trained pharmacy technician staff into a comprehensive, turnkey package. MUSC Health will also implement Omnicell's XT Series automated medication dispensing systems in patient care areas.

Additionally, we have secured several long-term partnership commitments with leading healthcare systems including St. Luke's University Health Network in eastern Pennsylvania and western New Jersey, plus Northern Arizona Healthcare, and in Charlotte, North Carolina-based Atrium Health. These health systems will support medication management across their service networks through Omnicell automation and intelligence solutions, helping to improve management of the pharmacy supply chain while empowering pharmacists, nurses, clinicians, and pharmacy staff to focus on patient and clinician satisfaction. These three health systems alone represent approximately 1% of the U.S. hospital market, based on total bed count.

For the second quarter we closed a record number of multi-million dollar deals versus any previous second quarter in the company's history. Over 80% of these deals are anchored by long-term commitments and over 90% of these customers will purchase multiple products from the Omnicell platform.

These are examples of how our business has expanded over the years from a single point solution to a platform of products and services, which has resulted in larger deal sizes across multiple product lines, more complex implementations and, we believe, a more comprehensive and enduring relationship with our customers.

The Autonomous Pharmacy is steadily evolving from a vision to a collaborative mission being driven in partnership with our customers and industry partnerships. I'm thrilled to share this progress and look forward to our continued success.

I will now hand the call over to Peter to discuss the second quarter financial results as well as the guidance for the second half of our fiscal year.

Our second quarter 2019 GAAP revenue of $217 million was up 15% over the second quarter of 2018. The increase in revenue was largely driven by:

1. An increase in XT Series implementations from a growing base of customers.
2. Increases in annual service and maintenance revenue from a larger installed base of equipment, and
3. Contributions from new products introduced over the past year.

The second quarter Earnings per share in accordance with GAAP was $0.37 per share, up from $0.16 per share in the second quarter of 2018. The increase in earnings per share is largely due to higher revenue in the second quarter of 2019 and achieving economies of scale over our operating expenses.

In addition to GAAP financial results, we report our results on a Non-GAAP basis which excludes stock compensation expense, amortization of intangible assets associated with acquisitions, acquisition and restructuring related expenses, tax reform and restructuring income tax benefits and expenses, contingent gains and amortization of debt issuance costs. We use Non-GAAP financial statements in addition to GAAP financial statements because we believe it is useful for investors to understand the effects of amortization of acquisition-related costs and non-cash stock compensation expenses that are a part of our reported results, as well as one-time events and acquisition and restructuring-related expenses. A full reconciliation of our GAAP to Non-GAAP results is included in our second quarter earnings press release and is posted on our website.

Second quarter 2019 Non-GAAP EPS was $0.67 per share, compared to $0.46 per share in the same period last year representing a 46% increase. Similar to the increase in our GAAP EPS, the increase in earnings per share on a Non-GAAP basis is, again largely due to economies of scale achieved in the context of higher revenue.
Non-GAAP other expenses for the second quarter of 2019 was $1.1 million compared to $2.8 million in Q2-18. The decrease primarily relates to lower interest expense as we have continued to deleverage.

Let’s now move to the balance sheet and cash flow.

Second quarter 2019 cash flow from operations was $27 million. Our operating cash flow in the second quarter was primarily driven by net income and adjustments for non-cash related items such as depreciation and amortization, which were partially offset by changes in working capital. During the second quarter of 2019 the Company generated approximately $12 million of free cash flow. We believe our business will continue to deliver free cash flow through the remainder of 2019.

Inventories at June 30, 2019 were approximately $104 million, flat from the previous quarter and flat from June 30, 2018. We’ve been able to hold our inventory relatively constant over the past year, despite continued growth, new product launches and larger average deal sizes.

Accounts receivable days sales outstanding for the second quarter were 87 days, down 6 days from the previous quarter and up 1 day from June 30, 2018. The decrease in DSO from last quarter is primarily due to higher sales.

As of June 30, 2019 our cash balance was $87 million, up $10 million sequentially and up $41 million from June 30, 2018. The increase in cash is due to proceeds from our At The Market offering and operating cash flows. During the second quarter we utilized our At The Market offering to sell approximately 217 thousand shares of our common stock at an average selling price of $82.51 per share. The total gross proceeds raised during the quarter was approximately $18 million. These proceeds were used to repay outstanding debt. During the second quarter we repaid $21 million of debt. As of June 30, 2019 we had $80 million of outstanding funded debt and our loan leverage measured as outstanding total funded loan balance over the Last Twelve Months (LTM) of bank EBITDA was approximately 0.5 times. As of June 30, 2019 we are now in a net cash position for the first time since closing the Aesynt transaction in early 2016.

Our headcount was 2,555 at June 30, 2019, up 83 from the end of the previous quarter and up 131 from the same quarter last year. The majority of the quarter increase is for manufacturing, implementation and service personnel needed to support our business as it continues to expand.

Moving to our full year 2019 guidance:

- We are increasing our full year product bookings guidance. We now expect 2019 Product Bookings to be between $765 million and $790 million. Our previous guidance was between $745 million and $780 million. The increase in our product bookings guidance is based on strong commercial momentum, especially from expected orders for our XT Series. We continue to gain traction in XT upgrades and as we have mentioned previously, we are in the early years of the XT upgrade cycle.
- We are increasing the midpoint of our 2019 Total Revenue guidance by narrowing our guidance range. We now expect 2019 Total Revenue to be between $886 million and $900 million. Our previous guidance range was $880 million and $900 million. The midpoint of our new guidance range is $893 million compared to $890 million which was the midpoint of the guidance range provided in our Q1-19 earnings call. Also, the midpoint of our new Total Revenue guidance implies approximately 13% year over year growth from our full year 2018 total revenue.
- This breaks down as follows:
- We now expect 2019 Product Revenue to be between $653 million and $663 million. Our previous guidance range was $652 million and $668 million.
- We now expect 2019 Service Revenue to be between $233 million and $237 million. Our previous guidance range was $228 million and $232 million.
- We are narrowing our total year 2019 Non-GAAP EPS guidance. We now expect 2019 Non-GAAP EPS to be between $2.65 and $2.82 per share. Our previous 2019 Non-GAAP EPS guidance range was between $2.62 and $2.82 per share. The midpoint of our new Non-GAAP EPS guidance implies approximately 31% growth year over year.

For the third quarter of 2019:

- We expect Total Revenue to be between $227 million and $233 million.
- We expect Product Revenue to be between $168 million and $173 million.

- We expect Service Revenue to be between $59 million Cand $60 million.
- We expect Non-GAAP EPS to be between $0.67 and $0.72 per share.

Finally, for 2019 we are assuming an average effective tax rate of 7% in our Non-GAAP EPS guidance range.

As Randall mentioned we are very pleased with the results for the second quarter of 2019 and we look forward to continuing to deliver profitable results throughout the rest of the year.

Thanks for joining us today. As we enter the second half of 2019, I'm thrilled to see our Autonomous Pharmacy vision coming to life. Together with our health system and retail pharmacy partners, we are helping to create value for the industry by transforming the pharmacy care delivery model, revolutionizing the way medications are delivered, reducing costs, and ultimately improving the lives of patients, clinicians and pharmacists.

I would like to thank our customers for partnering with us, and especially the Omnicell team for executing on our strategy as we deliver our vision of the Autonomous Pharmacy and improve healthcare for everyone!

Thank you everyone!

Omnicell, Inc.
Condensed Consolidated Statements of Operations
(Unaudited, in thousands, except per share data)

	Three months ended June 30,		Six months ended June 30,	
	2019	**2018**	**2019**	**2018**
Revenues:				
Product revenues	$ 158,379	$ 134,636	$ 303,989	$ 265,295
Services and other revenues	59,034	54,037	115,941	105,997
Total revenues	217,413	188,673	419,930	371,292
Cost of revenues:				
Cost of product revenues	84,583	75,076	163,394	150,493
Cost of services and other revenues	28,785	24,814	55,374	49,561
Total cost of revenues	113,368	99,890	218,768	200,054
Gross profit	104,045	88,783	201,162	171,238
Operating expenses:				
Research and development	16,848	15,512	32,926	32,049
Selling, general, and administrative	68,434	65,937	136,712	131,222
Total operating expenses	85,282	81,449	169,638	163,271
Income from operations	18,763	7,334	31,524	7,967
Interest and other income (expense), net	(1,629)	(896)	(3,039)	(3,625)
Income before provision for income taxes	17,134	6,438	28,485	4,342
Provision for (benefit from) income taxes	1,158	(150)	9,225	(4,966)
Net income	$ 15,976	$ 6,588	$ 19,260	$ 9,308
Net income per share:				
Basic	$ 0.39	$ 0.17	$ 0.47	$ 0.24
Diluted	$ 0.37	$ 0.16	$ 0.45	$ 0.23
Weighted-average shares outstanding:				
Basic	41,371	38,970	41,033	38,804
Diluted	42,945	40,000	42,646	39,854

Omnicell, Inc.
Condensed Consolidated Balance Sheets
(Unaudited, in thousands)

	June 30, 2019	December 31, 2018
ASSETS		
Current assets:		
Cash and cash equivalents	$ 87,482	$ 67,192
Accounts receivable and unbilled receivables, net	205,353	196,238
Inventories	103,906	100,868
Prepaid expenses	19,679	20,700
Other current assets	13,419	12,136
Total current assets	429,839	397,134
Property and equipment, net	52,847	51,500
Long-term investment in sales-type leases, net	21,041	17,082
Operating lease right-of-use assets	61,482	—
Goodwill	335,699	335,887
Intangible assets, net	134,101	143,686
Long-term deferred tax assets	31,195	15,197
Prepaid commissions	44,607	46,143
Other long-term assets	86,167	74,613
Total assets	$ 1,196,978	$ 1,081,242
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 40,183	$ 38,038
Accrued compensation	33,619	41,660
Accrued liabilities	54,570	43,047
Deferred revenues, net	83,012	81,835
Total current liabilities	211,384	204,580
Long-term deferred revenues	9,658	10,582
Long-term deferred tax liabilities	61,292	41,484
Long-term operating lease liabilities	55,237	—
Other long-term liabilities	9,603	9,562
Long-term debt, net	76,562	135,417
Total liabilities	423,736	401,625
Total stockholders' equity	773,242	679,617
Total liabilities and stockholders' equity	$ 1,196,978	$ 1,081,242

Omnicell, Inc.
Condensed Consolidated Statements of Cash Flows
(Unaudited, in thousands)

	Six months ended June 30,	
	2019	**2018**
Operating Activities		
Net income	$ 19,260	$ 9,308
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	25,874	24,829
Loss on disposal of property and equipment	399	—
Share-based compensation expense	16,670	13,766
Deferred income taxes	3,810	(6,655)
Amortization of operating lease right-of-use assets	5,226	—
Amortization of debt financing fees	1,145	1,145
Changes in operating assets and liabilities:		
Accounts receivable and unbilled receivables	(9,244)	15,476
Inventories	(4,466)	(9,789)
Prepaid expenses	1,021	2,126
Other current assets	(830)	(2,283)
Investment in sales-type leases	(4,412)	(1,838)
Prepaid commissions	1,536	2,812
Other long-term assets	3,061	(2,797)
Accounts payable	2,066	(12,229)
Accrued compensation	(8,041)	3,927
Accrued liabilities	1,810	(2,574)
Deferred revenues	253	5,336
Operating lease liabilities	(5,269)	—
Other long-term liabilities	3,891	167
Net cash provided by operating activities	53,760	40,727
Investing Activities		
Software development for external use	(22,581)	(13,091)
Purchases of property and equipment	(9,369)	(14,985)
Net cash used in investing activities	(31,950)	(28,076)
Financing Activities		
Repayment of debt and revolving credit facility	(60,000)	(12,500)
At the market offering, net of offering costs	37,806	—
Proceeds from issuances under stock-based compensation plans	25,333	16,117
Employees’ taxes paid related to restricted stock units	(4,722)	(3,062)
Net cash (used in) provided by financing activities	(1,583)	555
Effect of exchange rate changes on cash and cash equivalents	63	538
Net increase in cash and cash equivalents	20,290	13,744
Cash and cash equivalents at beginning of period	67,192	32,424
Cash and cash equivalents at end of period	$ 87,482	$ 46,168

Omnicell, Inc.
Reconciliation of GAAP to Non-GAAP
(Unaudited, in thousands, except per share data and percentage)

	Three months ended June 30,		Six months ended June 30,	
	2019	2018	2019	2018
Reconciliation of GAAP revenues to non-GAAP				
GAAP revenues	$ 217,413	$ 188,673	$ 419,930	$ 371,292
Non-GAAP revenues	$ 217,413	$ 188,673	$ 419,930	$ 371,292
Reconciliation of GAAP gross profit to non-GAAP gross profit:				
GAAP gross profit	$ 104,045	$ 88,783	$ 201,162	$ 171,238
GAAP gross margin	*47.9%*	*47.1%*	*47.9%*	*46.1%*
Share-based compensation expense	1,416	1,177	2,878	2,196
Amortization of acquired intangibles	2,044	2,756	4,110	5,547
Non-GAAP gross profit	$ 107,505	$ 92,716	$ 208,150	$ 178,981
Non-GAAP gross margin	*49.4%*	*49.1%*	*49.6%*	*48.2%*
Reconciliation of GAAP operating expenses to non-GAAP operating expenses:				
GAAP operating expenses	$ 85,282	$ 81,449	$ 169,638	$ 163,271
GAAP operating expenses % to total revenues	*39.2%*	*43.2%*	*40.4%*	*44.0%*
Share-based compensation expense	(6,844)	(6,061)	(13,792)	(11,570)
Amortization of acquired intangibles	(2,630)	(3,126)	(5,346)	(6,364)
Severance and other expenses	(440)	(1,735)	(726)	(3,247)
Non-GAAP operating expenses	$ 75,368	$ 70,527	$ 149,774	$ 142,090
Non-GAAP operating expenses % to total non-GAAP	*34.7%*	*37.4%*	*35.7%*	*38.3%*
Reconciliation of GAAP income from operations to non-GAAP income from operations:				
GAAP income from operations	$ 18,763	$ 7,334	$ 31,524	$ 7,967
GAAP operating income % to total revenues	*8.6%*	*3.9%*	*7.5%*	*2.1%*
Share-based compensation expense	8,260	7,238	16,670	13,766
Amortization of acquired intangibles	4,674	5,882	9,456	11,911
Severance and other expenses	440	1,735	726	3,247
Non-GAAP income from operations	$ 32,137	$ 22,189	$ 58,376	$ 36,891
Non-GAAP operating income % to total non-GAAP	*14.8%*	*11.8%*	*13.9%*	*9.9%*

Omnicell, Inc.
Reconciliation of GAAP to Non-GAAP
(Unaudited, in thousands, except per share data and percentage)

	Three months ended June 30,		Six months ended June 30,	
	2019	2018	2019	2018
Reconciliation of GAAP net income to non-GAAP net income:				
GAAP net income	$ 15,976	$ 6,588	$ 19,260	$ 9,308
Tax benefit for restructuring activity	—	—	—	(4,205)
Tax impact of IP restructuring	—	—	9,624	—
Share-based compensation expense	8,260	7,238	16,670	13,766
Amortization of acquired intangibles	4,674	5,882	9,456	11,911
Severance and other expenses[(a)]	1,013	2,308	1,872	4,393
Contingent gain	—	(2,456)	—	(2,456)
Tax effect of the adjustments above[(b)]	(1,194)	(1,204)	(2,378)	(2,907)
Non-GAAP net income	$ 28,729	$ 18,356	$ 54,504	$ 29,810
Reconciliation of GAAP net income per share - diluted to non-GAAP net income per share - diluted:				
Shares - diluted GAAP	42,945	40,000	42,646	39,854
Shares - diluted Non-GAAP	42,945	40,000	42,646	39,854
GAAP net income per share - diluted	$ 0.37	$ 0.16	$ 0.45	$ 0.23
Tax benefit for restructuring activity	—	—	—	(0.11)
Tax impact of IP restructuring	—	—	0.23	—
Share-based compensation expense	0.19	0.18	0.39	0.35
Amortization of acquired intangibles	0.11	0.15	0.22	0.30
Severance and other expenses	0.03	0.06	0.05	0.11
Contingent gain	—	(0.06)	—	(0.06)
Tax effect of the adjustments above[(b)]	(0.03)	(0.03)	(0.06)	(0.07)
Non-GAAP net income per share - diluted	$ 0.67	$ 0.46	$ 1.28	$ 0.75
Reconciliation of GAAP net income to non-GAAP Adjusted EBITDA[(c)]:				
GAAP net income	$ 15,976	$ 6,588	$ 19,260	$ 9,308
Share-based compensation expense	8,260	7,238	16,670	13,766
Interest (income) and expense, net	687	1,615	1,393	3,387
Depreciation and amortization expense	13,237	12,519	25,874	24,829
Severance and other expenses	1,013	2,308	1,872	4,393
Contingent gain	—	(2,456)	—	(2,456)
Income tax expense (benefit)	1,158	(150)	9,225	(4,966)
Non-GAAP adjusted EBITDA	$ 40,331	$ 27,662	$ 74,294	$ 48,261

(a) For the three months ended June 30, 2019, other expenses include $0.4 million and $0.2 million of amortization of debt issuance costs related to prior acquisitions and credit facilities amendments, respectively, and $0.4 million of tax restructuring costs. For the three months ended June 30, 2018, other expenses include $0.2 million of consulting-related restructuring expenses, and $0.4 million and $0.2 million of amortization of debt issuance costs related to prior acquisitions and credit facilities amendments, respectively.

(b) Tax effects calculated for all adjustments except tax benefits and expenses, and share-based compensation expense, using an estimated annual effective tax rate of 21% for both fiscal years 2019 and 2018.

[c] Defined as earnings before interest income and expense, taxes, depreciation and amortization, share-based compensation, as well as excluding certain non-GAAP adjustments.