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OVERVIEW:

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PRESENTATION

Xuyang Li - *Jefferies LLC, Research Division - Equity Analyst*

All right. Why don't we kick the session off. Good afternoon, everyone. Welcome to day 2 of the Jefferies New York Healthcare Conference. My name Xuyang Li, one of the med-tech analysts in the U.S. team. Really pleased to be joined by management from Cooper. We have Dan McBride, EVP and COO; and Kim Duncan, VP IR. So this would be a moderated Q&A session. Dan, Kim, welcome, and thanks for coming.

Daniel G. McBride - *The Cooper Companies, Inc. - Executive VP & COO*

Thank you.

QUESTIONS AND ANSWERS

Xuyang Li - *Jefferies LLC, Research Division - Equity Analyst*

So I guess, why don't we start with recent performance. You just reported results last week, solid beats on the top line and EPS. CVI leading the charge. Would be great maybe if you can talk a little bit about some of the growth drivers within the Vision Care business and what you're seeing in the market?

Daniel G. McBride - *The Cooper Companies, Inc. - Executive VP & COO*

Yes. Yes. So the vision market is really, really strong right now. Historically, we talked about the vision market as being a 4% to 6% grower. We're seeing it being in double digits and having been there for a couple of years now that we've done double-digit growth. The growth driver, the strongest one, clearly, is 1-day silicone hydrogels. Those are really taking off now. They represent about 57% of the 1-day market.

For comparison, FRP is 87% of the silicon hydrogel market for monthly and 2 weeks. So there's still a lot of growth room to go there. Underneath that, torics and multifocals are really leading the charge. Torics have always been historically been underpenetrated in the marketplace, and now we're starting to see more and more markets expand how much they fit. So that's great.

Quality of the multifocal products has improved. So that's helping sort of older wearers that want to stay in contact lenses. The other driver sort of in the vision care market just for us really is myopia management is helping at kind of a point of growth. And that's adding just a whole new space and expanding the category.

Xuyang Li - *Jefferies LLC, Research Division - Equity Analyst*

All right. Great. That's a nice overview. I guess maybe just on the daily SiHy growth continues to be really strong at 17%. How high do you think penetration can get for that product category?

Daniel G. McBride - *The Cooper Companies, Inc. - Executive VP & COO*

Yes. I look to that and I go, we have -- obviously, FRP space, I just said, was at 87%. Vision the 1-day space probably doesn't quite get there because you need full participation of the market to get there. And right now, we still have the MOIST family, which is the largest sort of 1-day family in hydrogels. And there isn't really a clear trade-up that J&J has put together for that. So I think, eventually, you could see the 2 mirroring, but I would say sort of the near term out would be more like seeing 1-day SiHy getting up into the mid-70s or somewhere in that range of the category.

Xuyang Li - *Jefferies LLC, Research Division - Equity Analyst*

All right. Great. I guess in terms of capacity, there's been some shortages. How impactful are the capacity issues? How long do you think you can continue? It seems like it could go on for several years as we wait for more supply to come online. How much are you increasing capacity to meet the increased demand?

Daniel G. McBride - *The Cooper Companies, Inc. - Executive VP & COO*

Yes. So the whole industry has been facing capacity shortages. Part of it is just really, really strong post-pandemic demand way above sort of normal trends. For us, we're looking to -- we're improving every month. I would say that we're -- with additional capacity coming online, we should be out of really pretty much the whole situation in early 2024, somewhere in the first half there. When I think about it in terms of capacity, we historically tried to build capacity about 10% above what we forecasted growth.

We've now kind of modified our capacity plans to go 20% above to kind of handle the additional demand and make sure that we're not missing out on opportunity. When I think about it from an industry perspective, I think we've got a long-term strong capacity demand, largely because as we phase out sort of these large 1-day hydrogel families, that requires new capacity to come in.

So there's both capacity to grow the market, but there's also capacity to replace the existing capacity that exists in hydrogel. So right now, what I'm happy to say is that I think there's noise around service for at least our business for Cooper Vision's business is really low right now. And I think it's going to get way better. I don't really have insights on where competitors are in their supply chain problems.

Xuyang Li - *Jefferies LLC, Research Division - Equity Analyst*

Okay. Got it. I guess kind of an unfair follow-up. But just kind of curious, I mean, your increase in capacity, others as well. I know you just said you don't have visibility into their plans. But conceptually, what do you think about the risk of potentially oversupply?

Daniel G. McBride - *The Cooper Companies, Inc. - Executive VP & COO*

Yes. I think the risk there is probably pretty low, one, because I think we're actually -- I think the industry is more likely to undershoot demand. And that's because I think it's not fully factoring in all of that trade up of the 1-day hydrogels that needs to be taken in. But the other reason is, is because even when we look at increasing our capacity, we're doing it in a way that is really incremental. So if I look at it, even if we over buy by a year, then we basically just don't put in service for that period of time.

But we easily get into the area that we're consuming. With the type of numbers that we're doing in CapEx, we're not buying multiple years' worth of excess capacity. We're just buying incremental to what we see the need for when the CapEx numbers I have visibility to from competitors suggest they're doing the same.

So I don't really see the industry getting into an oversupply situation. And to the extent that there may be some of that going on, I think it can easily be absorbed in the course of a year or 2 easily.

Xuyang Li - Jefferies LLC, Research Division - Equity Analyst

Okay. Great. So we get asked a lot about the risk of extended wear or trade downs from consumers if there is an economic slowdown. The annual cost of daily SiHys is higher. I guess -- just kind of curious, what are your thoughts on extended wear and trade downs and how bad does the employment rate has to get for this to be a real risk?

Daniel G. McBride - The Cooper Companies, Inc. - Executive VP & COO

Yes. And I think that's the crux of your question there is the key point, which is I don't think we see anything unless we see a real strong uptick in unemployment. Because right now, what we're seeing from consumer behavior is they're still buying all the top end products. And there -- so there's no behavior in the marketplace that suggests there's any kind of trade down or extending of usage of lenses. Beyond what is normal in the marketplace. I would think it would have to get pretty bad. So when you think about 2008, which was really just truly awful, the industry grew 3%.

So we're nowhere near any of that. I don't think we're seeing that coming down. We're certainly not seeing into the marketplace today. So I'm pretty bullish that even in a mild recessionary situation, the industry may just plow through it without really noticing it.

Contact lenses are not discretionary items for the people that wear them. They're kind of consumer essentials. So they're pretty low on the list of where consumers cut.

Xuyang Li - Jefferies LLC, Research Division - Equity Analyst

All right. Got it. So I guess just maybe on the guidance. So just given the fiscal Q2 results, you increased the guidance by slightly more than the beat. I guess how conservative is the updated guidance given some of the drivers for growth, daily SiHys, myopia management, fertility should continue to grow fairly strongly? Where do you see the biggest sources of upside? What are some of the biggest risks outside of some maybe tailwind macro issues?

Daniel G. McBride - The Cooper Companies, Inc. - Executive VP & COO

Yes. So when I think about -- we try and put guidance right in the midst of our risk. And so that's how we try and guide. What's unique about this kind of guidance is if we looked at what we saw in the industry, we'd definitely be going on the high side of guidance. So what's going on in the other side of guidance really is more of a qualitative concerns about the macro environment, what we're we gave guidance, we were just in the middle of the debt ceiling crisis. We hear a lot about is the Fed going to really slow the economy down.

So there's elements of it that are very qualitative. So in a way, -- it's not the normal way we would balance the midpoint of guidance for the Vision business. And so if I go on what I'm seeing in the marketplace, I'm very bullish on the guidance range. But I do think it was fair to kind of put that caution in. When I think about the drivers, it's clearly -- 1-days are really strong. Torics are strong what we talked about. We're seeing a good, steady growth in myopia management.

So those are all really, really positive. If I think what really puts us to the other side of the guidance range are really, again, it gets to -- to me, it gets to probably the clearest indicator would be unemployment. It would be something like that, that really shocked the consumer into a fairly fast change in behavior because you're only talking about the second half of the year, and there's not that much time left to really impact how the market is moving.

Xuyang Li - Jefferies LLC, Research Division - Equity Analyst

All right. Great. So I guess a key differentiator for the company is the much higher number of SKUs you can offer. Does that imply Cooper's natural market share can or should be higher than it is today?

Daniel G. McBride - *The Cooper Companies, Inc. - Executive VP & COO*

I would like to think so. I mean, I definitely think it's a key differentiator. When I talk about the industry, one of the things that I try and expressed to investors is, is that oftentimes, you look at the companies and you say, Apple, Apple, Apple were all kind of the same. But our competitors who have great strategies, they're doing fine. They really serve a bulk of the market, but around 100,000 SKUs is what they're putting into the marketplace.

We actively provide 8 million SKUs into the marketplace. So we're really doing Apple, Apple Orange. We're doing something different. And so those edges of the bell curve, they're not very big, but we're not sharing that with anybody where whatever is there is 100% going into Cooper because there is no competitive product. Where it's relevant is kind of almost less on the aggregate numbers than it is on what it means to a practice that wants to use those -- the full range of SKUs.

Because if you fit a toric, torics up fitting characteristics, our toric fits slightly different than Alcon's. Alcon's fits slightly different than J&J. J&J fits different than Bausch. So if an ECP is using your product to use the full range, you get a halo effect back into the core of the range because they're just used to fitting -- they're used to the fitting characteristics. They're used to how the lens spins on the eye. They're used to how to adjust when a consumer says, "Hey, I'm not really getting the full benefit of my vision.

So we kind of view that extended range is not only providing us a little bit of extra potential for share, but it's also a way of making us more relevant and more meaningful to the ECPs. So yes, I do think we should have a greater share. And I think the one that's going to be really telling that I'm most excited about is MyDay toric because we've just changed the 1-day category. 1-day category was always just a very center of the bell curve, very easy, cheap to serve piece of the marketplace, and we're giving the full range of the Biofinity toric and the MyDay toric, which allows the ECPs to just have a customer come in and say which more out do you want to be in? You want to be an FRP or 1-day, I can do both. And I think that's going to be a big difference, and it's exciting from our perspective.

Xuyang Li - *Jefferies LLC, Research Division - Equity Analyst*

All right. Great. Maybe switching gears to myopia management. So strong growth in the quarter, despite some weakness in China. I was wondering if you can talk about what's driving the inflection in growth last quarter?

Daniel G. McBride - *The Cooper Companies, Inc. - Executive VP & COO*

Yes. And I think what's really driving myopia management is that two things. One, really, the industry is fully behind it now. There's been a clear shift over the last few years. The existence of detractors around myopia management is really, really gone. They're really just our supporters and neutral, and there's this big vast group of neutral. And with that shift, we've also kind of shifted our strategy to realize what we need to do is double down on the supporters and really focus our selling effort on building that base and showing that there are really truly great business success stories about building a myopia management practice.

And retention rates are in the 90 percentile. So I mean people that are investing in it are getting patients in. They stay in it for 4 to 7 years, whatever the growth of the eye that they're dealing with, and then they're layering on more and more into their practice. So what I think is exciting about it is that we're seeing a real strong base being built. We're seeing the large spectacle companies, which really are the dominant players in the industry getting into myopia management.

Essilor with Stellest, Hoya with Miyosmart. So you're seeing the whole industry buying into this idea that myopia management should be a treatment for children and it's on its pathway to getting it to be a treatment or a standard of care.

Xuyang Li - Jefferies LLC, Research Division - Equity Analyst

All right. Maybe if you can talk a little bit about the potential halo effects of MiSight. It's a very differentiated product. Is it opening new doors and new accounts for you? Does it enable deeper penetration into existing accounts?

Daniel G. McBride - The Cooper Companies, Inc. - Executive VP & COO

Yes. What's interesting there is that the -- we know all the accounts, everybody knows all the accounts. There's not -- it isn't a new group, but there are accounts that do more business with our competitors, less than us. When they're entering into myopia management, we're bringing them something unique, a new business, a new way of driving revenues within their practices.

It definitely is opening the doors to different conversations with them about other products we're bringing in, like, at the same time, bringing in MyDay toric, which a full range of torics on the 1-day side. So we're definitely seeing it open doors. We're allowing -- it's giving us a way of deepening the relationship. It's allowing a different conversation to happen with the salespeople. It's not just filling out the empty trial sets and talking about the next iteration of sphere. It's talking about something that's meaningful change within their businesses.

And that's a great opening for a salesperson to be able to also then talk about other products in the portfolio. Certainly, when we look at numbers, the myopia management practices actually have a higher growth rate than the non-myopia management practices for us. So that's anecdotally pretty decent evidence that there's a halo effect to this.

Xuyang Li - Jefferies LLC, Research Division - Equity Analyst

All right. That's good to hear. So I guess how has MiSight's impact been, bringing some of the younger consumers to the Cooper portfolio of contact lenses?

Daniel G. McBride - The Cooper Companies, Inc. - Executive VP & COO

Yes. That's probably the biggest upside to practitioners and to the industry. The average age of people going into contact lenses is 17 years old. The average age of people going into myopia management is 10. So there's 7 full years of additional contact lens wear right there. So it's a pretty big deal. It's still a small product family, but it's really changing perceptions in parents and in ECPs minds of what age can kids go into contact lenses.

Because I would have said 15, the data says 17. But certainly, it was nowhere near 10.

Xuyang Li - Jefferies LLC, Research Division - Equity Analyst

All right. Great. A lot of runway there. I guess in terms of just the guidance, \$120 million to \$130 million. It seems like there could be some upside to those numbers. I was wondering -- I'm not sure if you have broken out before, but how much of that is tied to China? And longer term, how big do you think the China MiSight market can be relative to the U.S. or Europe?

Daniel G. McBride - The Cooper Companies, Inc. - Executive VP & COO

Yes. And we really aren't breaking out individual markets on myopia management. The couple of things I would say is, is that we're not expecting anything extraordinary from China in that \$120 million to \$130 million. We're expecting kind of a back half normal China market, which is kind of what we're seeing right now as they pull out of COVID. And when we think about China, the other point that I would just point out is, is that China is much more of an ortho-k myopia management market.

So MiSight's build in there will be a bit slower as it kind of brings that product on. But it's a good market for us. We're not projecting a lot of upside out of China and maybe that will help us get some upside on our guidance range.

Xuyang Li - Jefferies LLC, Research Division - Equity Analyst

Okay. Great. Let's see -- sorry, having some technical issues here. I guess I wanted to switch gears a little bit and talk about the -- on the surgical business. I wanted to hear a little bit about what do you think the performance was in the quarter relative to your expectations? And maybe just talk about some of the key drivers of that business?

Daniel G. McBride - The Cooper Companies, Inc. - Executive VP & COO

Yes. We're really excited about the performance on the surgical side, particularly fertility. I mean they've done now 11 straight quarters of double-digit growth. And that's a business that has a tremendous amount of upside. If you think about what's going on with birth rates globally and birth rates in countries, I think you not only have upside just in terms of the dynamics of couples. I think you have upside in terms of the dynamics of governments as they try and figure out how to deal with declining birth rates in their country.

So that's a super exciting space. We were really pleased with office and surgical. That was strong growth for there. There's a little bit of that is catch up on back orders, but it was still a really strong. Disappointed in PARAGARD, but we feel like that product still will be able to put out low single digits for the year, a little slower recovery after the price increase in Q2 than we had expected.

But overall, really happy with that business. It now is solidly able to organically grow both in the office and surgical side and the fertility side. So that's a good positioning for it to be in.

Xuyang Li - Jefferies LLC, Research Division - Equity Analyst

All right. Great. I think in terms of PARAGARD growth, a lot of that is driven by price. I guess, can you comment on how much additional price you can take annually going forward?

Daniel G. McBride - The Cooper Companies, Inc. - Executive VP & COO

Yes. So we took an 8% price increase this year. We're not really seeing unit growth in IUDs at all. Hormonal [or are]. So we don't have full insight into what goes on in the hormonal market. So our projection is, is that we're not going to see much, if any, unit growth in PARAGARD and it will come in price. We will evaluate price just annually. Probably, the biggest proxy that we'll look to is what's going on with the price changes in the hormonal IUDs.

But we haven't given guidance on where we might take price. And largely, it's going to be just watching the market and seeing what's going on with inflation, what's going on with pricing and hormonal IUDs and then the general device market.

Xuyang Li - Jefferies LLC, Research Division - Equity Analyst

And I guess just in light of the Cook Medical updates, what are your latest thoughts on M&A? Would it be focused on surgical? Should we see something on the vision side as well? Maybe you can talk about sizes of deals as well?

Daniel G. McBride - *The Cooper Companies, Inc. - Executive VP & COO*

Yes. So on M&A, we have targets on both sides. There's obviously more things to buy on the surgical side with a fairly concentrated industry on the vision side. It's more difficult to get acquisitions done. So we'll continue to be active in M&A ideally more towards fertility, but both sides of the surgical business. Size of deals, obviously, we have higher levels of debt and interest rates are higher.

So the hurdle rate and that any acquisition needs to make is going to be higher just to make sure that it's accretive and delivers the kind of return that we want. When I think about uses of capital, investing in the business and debt paydown are kind of our top two priorities, but M&A is still going to be a piece of what we do.

Xuyang Li - *Jefferies LLC, Research Division - Equity Analyst*

All right. Great. I guess maybe on margins. What are some of the bigger macro drivers for gross margin expansion? Daily SiHys are very margin accretive. How do you expect that to play out in the next few years? Are there other key gross margin drivers as well to highlight?

Daniel G. McBride - *The Cooper Companies, Inc. - Executive VP & COO*

Yes. So when we think about gross margin, you -- clearly, there's the continuous improvement programs that we're running through, better lines, getting the lines fully up to speed. That largely has been offsetting some of the headwinds that we've been facing and higher labor costs, higher raw materials cost. So it kind of says we can do slightly better on gross margins, but we're kind of in that range.

1-days in general are dilutive to gross margins. And so we hurdle that really through a lot of the cost improvement programs that we're doing. But -- so we see at least for the end of the year, trending to the upper 66%, and we haven't yet guided further out on where we're going to -- where we think the overall gross margins will go.

Xuyang Li - *Jefferies LLC, Research Division - Equity Analyst*

All right. Great. And I guess in the less than 1-minute time we have kind of a question out of left you. I was kind of wondering, how do you think ChatGPT or generative AI can impact the industry and Cooper's businesses? Can it increase efficiency or decrease costs?

Daniel G. McBride - *The Cooper Companies, Inc. - Executive VP & COO*

Yes. So in terms of AI, the only really direct line on AI is, is we obviously use AI in our genetic testing to deliver better outcomes and results. So that is like sort of what you would call your -- like your direct product use of AI. If I think of AI otherwise within the business, we're going to be more of a consumer of AI improvements that go through.

And obviously, there's lots of analytics that we use, both in the manufacturing and distribution and other places. So I think it's a net positive for cost and being able to drive cost out of the system. But it's not that you're going to see Cooper really driving new AI-driven products or AI innovations other than maybe in the genetic testing space where it's -- where we actually are active in that.

Xuyang Li - *Jefferies LLC, Research Division - Equity Analyst*

All right. Great. I think that's all the time we have. Dan and Kim, thanks for coming, and thanks for the great discussion.

Daniel G. McBride - *The Cooper Companies, Inc. - Executive VP & COO*

Thank you.

Kim Duncan - *The Cooper Companies, Inc. - VP of IR & Risk Management*

Take care. Thanks, everybody.

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