

# Q4 FY21 Cardinal Health, Inc. Earnings Conference Call

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Operator: Good day, and welcome to the Cardinal Health, Incorporated Fourth Quarter Fiscal Year 2021 Earnings Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Vice President of Investor Relations, Kevin Moran. Please go ahead, sir.

Kevin Moran: Good morning, and welcome. Today, we will discuss Cardinal Health's Fourth Quarter Fiscal 2021. Results along with guidance for fiscal year 2022. You can find today's press release and presentation on the IR section of our Website at [ir.cardinalhealth.com](http://ir.cardinalhealth.com).

Joining me today are Mike Kaufmann, Chief Executive Officer; and Jason Hollar, Chief Financial Officer. During the call, we will be making forward-looking statements. The matters addressed in the statements are subject to the risks and uncertainties that could cause actual results to differ materially from those projected or implied. Please refer to our SEC filings and the forward-looking statement slide at the beginning of our presentation for a description of these risks and uncertainties.

Please note that during the discussion today, our comments will be on a non-GAAP basis unless they are specifically called out as GAAP. GAAP to non-GAAP reconciliations for all relevant periods can be found in the schedule attached to our press release.

During the Q&A portion of today's call, we please ask that you try and limit yourself to one question so that we can try and give everyone an opportunity. With that, I will now turn the call over to Mike.

Mike Kaufmann: Thank you, Kevin, and good morning, everyone. I will start my comments today by acknowledging that our fourth quarter results were below our expectations and yours primarily due to an inventory reserve adjustment of \$197 million. This reserve adjustment was driven by changing market conditions related to COVID-19 on certain highly commoditized PPE products.

To meet our customer commitments during the pandemic, we carried higher levels of inventory in certain PPE categories during a period of significantly increased demand, higher prices and longer-than-normal supply chains. Our analysis at the quarter end of both the anticipated customer demand and projected future sale prices for these products resulted in a sizable inventory reserve that affected a subset of our medical products inventory.

In addition, there were a few other unexpected items that affected our results, which Jason will cover in his remarks. Throughout the past year, we have been taking action to drive performance, and we will continue to move forward with urgency. For example, we divested the Cordis business, extended our Red Oak Sourcing agreement with CVS Health, identified \$250 million of additional cost savings opportunities, restructured parts of our organization to increase accountability and made important leadership changes. We are continually reviewing our business and seeking areas to improve.

With the actions we've taken to date and our plans for FY '22, we feel confident in our strategy and are encouraged by the tailwinds behind our growth areas and strong cash flow generation.

In FY '21, we grew revenue 6% versus the prior year and despite an estimated \$200 million year-over-year operating earnings headwind related to COVID-19, we grew EPS. We continue to aggressively streamline our cost structure and surpassed our enterprise cost savings target for the third consecutive year. We generated strong operating cash flow, prioritized returning cash to shareholders through dividends and share repurchases and took actions to further strengthen our balance sheet.

As I reflect on the unprecedented events of the past year, our team has prioritized our customers, maintained continuous operations, partnered with governmental agencies to support vaccine administration and protect patients, and has further improved the resiliency of our supply chain.

Before turning it over to Jason, I want to highlight last week's announcement that we have negotiated a comprehensive proposed settlement agreement and settlement process designed to achieve broad resolution of governmental opioid claims. If all conditions are satisfied, this agreement would result in the settlement of a substantial majority of opioid lawsuits filed by state and local governmental entities, and depending on the level of state and subdivision participation, we would pay up to \$6.4 billion over 18 years. This is an important step forward for our company.

As we've consistently said, we remain committed to being part of the solution for the U.S. opioid epidemic and believe the settlement would be a prudent way to provide necessary relief to our communities and certainty for our shareholders.

With that, I'll turn it over to Jason to further discuss our results and FY '22 guidance.

Jason Hollar: Thanks, Mike, and good morning, everyone. In the fourth quarter, we delivered EPS of \$0.77, which as Mike mentioned, included a \$197 million inventory reserve on certain PPE in the Medical segment.

Turning to the Pharma segment on slide six. Fourth quarter revenue increased 15% to \$38 billion, driven primarily by sales growth from large Pharmaceutical Distribution and Specialty Solutions customers. As a reminder, the fourth quarter of fiscal '20 included reduced pharmaceutical demand related to COVID-19, which, to a lesser extent, contributed to the growth in the quarter.

Pharma segment profit was flat in the fourth quarter at \$358 million. This reflects COVID-19-related volume recovery in our Nuclear business, offset by Pharmaceutical Distribution customer contract renewals. This impact from renewals was in line with our expectations and generally consistent with prior quarters. However, there were some other items, including inventory adjustments and opioid-related legal costs that were higher than previously assumed.

As we've mentioned, we continue to prioritize investing for growth and optimizing our core operations. In the fourth quarter, the deployment of some of these technology enhancements resulted in incremental costs for implementation and depreciation, which we also expect the next several quarters as we continue to deploy new capabilities.

I will further discuss our investments as we look to fiscal year '22.

As we highlighted last quarter, we continued to experience softer volumes in certain therapeutic classes within our generics program. Our generics program continued to see generally consistent market dynamics. With respect to other product types, including brand, specialty and consumer health, we largely saw volumes at or above pre-pandemic levels during the fourth quarter.

In Medical, depicted on slide seven, revenue increased 23% to \$4.2 billion in the fourth quarter. This revenue increase was driven by a net positive impact from COVID-19 on products and distribution, primarily due to a recovery in elective procedure volumes and a positive PPE pricing impact. Medical segment loss of \$63 million in the fourth quarter was due to an adverse impact from COVID-19, primarily due to the previously mentioned inventory reserve, partially offset by a recovery in elective procedure volumes. Additionally, benefits from cost savings initiatives were offset by elevated supply chain costs.

During the quarter, we were encouraged to see elective procedure volumes effectively return to near pre-COVID-19 levels. While our team continued to execute on our cost savings and efficiency initiatives within our global manufacturing and supply chain, we did experience elevated supply chain costs, particularly in the areas of freight, labor and commodities. We are taking actions to help mitigate these impacts. But as we look forward, we do expect some of these higher costs to continue into next year.

Now I'll transition to full year results, beginning with the enterprise. Total company revenue increased 6% to \$162 billion with strong top line growth in both segments. Consolidated gross margin decreased 2% to 66.8%. Despite sales growth, SG&A decreased 1%, reflecting the benefits of our enterprise-wide cost savings measures. Operating earnings decreased 5%, reflecting a headwind of approximately \$200 million year-over-year related to COVID-19, which was split fairly evenly between the segments. Excluding COVID-19, operating earnings would have grown in the low single digits in fiscal '21.

Moving below the line, interest and other decreased 44% to \$133 million, driven by multiple items, including lower interest expense from debt reduction actions, an increase in the value of our deferred compensation plan and one-time investment gains. As a reminder, deferred compensation gains or losses reported in interest and other are fully offset in corporate SG&A and net neutral to our bottom line.

Our annual effective tax rate finished at 22.8%, benefiting from discrete items. We finished the year with EPS of \$5.57, reflecting growth of 2% despite the net COVID-19 headwind.

Turning to the balance sheet. We continue to operate with high net working capital efficiency, generating robust operating cash flow of \$2.4 billion for the full year. We finished the year with a strong cash position of \$3.4 billion, with no outstanding borrowings on our credit facilities.

As a reminder, the day of the week in which the quarter ends affects point-in-time cash flows. We continue to deploy capital according to our priorities, investing \$400 million back into the business in capex to drive organic growth, strengthening our balance sheet through approximately \$550 million in debt paydown, which occurred primarily in the fourth quarter and returning nearly \$800 million to shareholders through dividends and share repurchases.

As for the segment's full year results, beginning with Pharma on slide 10... Pharma revenue increased 6% to \$146 billion, driven by sales growth from Pharmaceutical Distribution and Specialty Solutions customers. Pharma segment profit decreased 4% to \$1.7 billion due to volume declines in the company's generics program, including the impact of COVID-19. This was partially offset by favorable brand sales mix. Excluding COVID-19, we estimate the Pharma segment would have grown low single digits in fiscal '21.

Turning to Medical on slide 11... Full year Medical revenue increased 8% to \$16.7 billion, driven by a net positive impact from COVID-19 on products and distribution. As we saw throughout the year, this increase was primarily due to the impact of PPE sales and higher volumes in our Lab business. Medical segment profit decreased 13% to \$577 million due to an adverse impact from COVID-19 on products and distribution. This was primarily due to the fourth quarter inventory reserve on certain PPE products, partially offset by higher volumes in our Lab business. Additionally, the team delivered strong cost savings, including global manufacturing efficiencies on the year.

When adjusting for COVID-19-related impacts in Medical, we estimate the segment would have grown mid-single digits for the full year. While our fiscal '21 results fell short of our expectations, the underlying growth we saw in both segments, excluding COVID-19, gives us confidence as we move into next year and the pandemics effects on our businesses continue to dissipate.

Turning to our guidance for fiscal '22 on slide 13... We expect earnings per share in the range of \$5.60 to \$5.90. This reflects incremental technology investments of approximately \$120 million to drive growth and efficiencies across the enterprise, the Cordis divestiture and other assumptions that we will detail momentarily. We expect interest and other in the range of \$150 million to \$180 million. We anticipate continued reduction in interest expense, with the increase over the prior year primarily a result of the fiscal '21 capability in deferred compensation not expected to repeat.

We are assuming a non-GAAP effective tax rate in the range of 23.5% to 25.5%. We expect diluted weighted average shares outstanding in the range of \$287 million to \$292 million, and capex of \$400 million to \$450 million.

Transitioning to the segments, beginning with Pharma on slide 14... We expect high single-digit revenue growth driven by growth from large customers and continued COVID-19 recovery and mid-single-digit segment profit growth. We anticipate COVID-19 will be an overall tailwind of approximately \$100 million to Pharma segment profit compared to the prior year. While we will likely continue to see some choppiness, we expect volume recovery in certain generic therapeutic classes by the end of the calendar year.

As mentioned, we are investing in technology enhancements to drive growth and efficiencies, which we expect will lead to an \$80 million segment profit headwind in fiscal '22, including the annualization of the investments made in the fourth quarter.

Adjusting for the COVID-19-related impacts and the incremental technology investments, we see Pharma normalized growth in the low to mid-single-digit range. We believe normalizing for these impacts provides a better approximation for the long-range growth trajectory of the business.

As for other assumptions, we continue to expect consistent market dynamics in our generics program. We expect increased contributions from our growth areas, specialty, including biosimilars,

nuclear and outcomes. We anticipate a similar contingent brand inflation rate as in fiscal '21 with continued less dollar contribution each year. And we expect opioid-related legal costs of approximately \$125 million, an increase of \$10 million versus fiscal '21.

For Medical on slide 15... We expect revenue to be approximately flat in fiscal '22, primarily due to the prior year COVID-19 comparison with low double-digit segment profit growth. With respect to COVID-19, we expect an approximate \$100 million year-over-year tailwind to Medical segment profit. We are assuming elective procedures to remain at or near pre-COVID levels for the duration of the year. We expect moderate headwinds in fiscal '22 related to timing of selling higher-cost PPE products and lower lab testing utilization versus the prior year. And we anticipate a year-over-year comparison benefit related to the PPE inventory reserve.

Outside of COVID-19, we expect an approximate \$80 million impact to segment profit due to the Cordis divestiture. Note, the anticipated reported impact for fiscal '22 is higher than previously communicated, primarily due to exchange rate favorability and other operating improvements within the business in the prior year. Additionally, we expect to invest an incremental \$20 million in technology enhancements in our at-Home business to drive growth and efficiencies. Adjusting for these items, we see normalized Medical segment profit growth of mid to high-single digits in fiscal '22.

Finally, as seen in the fourth quarter, we expect elevated supply chain cost to persist, particularly in the first half of the year. We anticipate these elevated costs will be partially offset by the continued benefits from our global manufacturing and supply chain transformation, which will ramp up throughout the year.

Now a few additional comments on the expected cadence next year. We expect profit growth to be significantly back-half weighted in both segments. In Pharma, this is primarily driven by the timing of the previously mentioned incremental technology investments being more weighted towards the front half as well as stronger expected second half performance in our generics program, including the impact of COVID-19.

In Medical, in addition to the elevated supply chain costs, we also anticipate the total unfavorable fiscal '22 COVID-19 impact of approximately \$50 million to occur primarily in the first half of the year. As a reminder, we also experienced favorable COVID-19 impact in the first half of fiscal '21, which was of a similar magnitude.

Across the organization, we continue to place a high priority on cash flow generation as well as allocating capital in a balanced, disciplined and shareholder-friendly manner. Our strong cash flow and improving capital position will enable our capital allocation priorities, support our company's obligations and provide increased flexibility and the ability to be more opportunistic in our capital deployment.

Along those lines, we anticipate deploying the Cordis proceeds through a combination of share repurchases and debt paydown, which is expected to offset the earnings dilution on a pro forma basis. We expect share repurchases in the range of \$500 million to \$1 billion in fiscal '22. In addition, we expect total debt paydown of approximately \$850 million, reflecting the completion of the remaining June 2022 debt tower at or before maturity.

With that, I'll now turn it over to Mike.

Mike Kaufmann: Thanks, Jason. To be clear, we are disappointed with this finish to the year and are moving forward for the sense of urgency to improve our operation and execute our strategy. We're prioritizing investments in our strategic growth areas and expect these businesses to collectively realize double digit growth in FY '22. And across our business, we're enhancing our IT infrastructure in key areas to increase capabilities and digitization, improve the customer experience and drive productivity. While we expect to benefit from these investments this fiscal year, the majority of these benefits will materialize in FY '23 and beyond.

In Pharma, we're investing an additional \$80 million in technology infrastructure to create additional operational efficiencies, improve data insights and drive cost synergies to enhance our ability to grow and generate better outcomes for our customers.

Our generics program remains a critical priority. This week, we extended our Red Oak agreement with CVS Health for an additional five years, which takes the term of our generic sourcing joint venture through June 30, 2029. This ensures that we can continue to deliver best-in-class sourcing capabilities for our customers well into the future. We are also investing in data and analytics, including our pricing capabilities, as we continue to focus on managing all components of our generics program and expect market dynamics consistent with the last few years.

We remain committed to supporting the retail pharmacy community. At our recent Annual Retail Business conference, we connected virtually with over 4,000 retail independent pharmacy customers and launched two new digital offerings, NavixRx and e-commerce storefront to help independent pharmacies expand their services and improve health care outcomes.

In Specialty, we're investing in our Sonexus™ patient hub where our technology solutions help biopharma customers remove barriers to patient care. In our third-party logistics business, we're expanding our cold chain storage space to accommodate the growing number of temperature sensitive products, including cell and gene therapies.

In Nuclear, we received FDA approval to use our radioactive diagnostic agent LYMPHOSEEK®, in pediatric patients one month and older. We continue to build out our multi-million-dollar center for Theranostics advancement in Indianapolis and are also investing to expand our PET capabilities. We expect double-digit profit growth in Nuclear over the next several years. And in outcomes, we also expect double-digit profit growth as we expand our direct-to-patient digital footprint and implement new patient adherence programs.

Turning to Medical. We have been taking quick, decisive action throughout the fiscal year to streamline and simplify our Medical business, and this work remains a top priority heading into FY '22. We've recently restructured our organization to establish clearer lines of ownership and accountability, and made some management changes, including appointing a single leader to manage U.S. medical products and distribution as well as a single leader to manage international.

With the divestiture of Cordis, we plan to significantly reduce our international commercial footprint and have initially identified 36 markets we intend to exit, so we can focus on the locations where we have a competitive advantage and can generate sustained long-term growth.

We're laser-focused on enhancing supply chain resiliency, improving business continuity and investing in advanced planning capabilities to drive forward-looking insights to better serve our customers and their patients.

In addition, our Medical Services businesses, OptiFreight® Logistics and WaveMark continue to enable clinically integrated and digitally automated supply chains. Our At-Home business continues to focus on enabling and supporting comfortable home-based care for patients with acute and chronic conditions. We continue to see volume growth as care is rapidly shifting to the home.

For FY '22, we're investing an additional \$20 million in technology infrastructure to create operational efficiencies and better data visibility.

With respect to the Enterprise, we're aggressively reviewing our cost structure to continue streamlining our operations and processes and intend to reinvest a portion of these savings to fuel future growth. In FY '22, we plan to launch initiatives that will deliver at least an additional \$250 million savings by FY '23.

As Jason discussed earlier, we take a balanced, disciplined and shareholder-friendly approach to capital deployment with a focus on investing in the business, maintaining a strong balance sheet and returning cash to shareholders.

In closing, I want to thank our employees for their hard work and contributions that make it possible for Cardinal Health to fulfill its mission of improving the lives of people every day. And now Jason and I will take your questions.

Operator: Thank you. And if you would like to ask a question, please signal by pressing star 1 on your telephone keypad. If you are using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Once again, everyone, to ask a question, please press star 1 on your telephone keypad. We'll pause for a quick moment to assemble the queue.

And our first question will come from Michael Cherny with Bank of America. Please go ahead.

Michael Cherny: Good morning, thanks so much for the question. I want to dive a little bit more into the capital deployment priorities as you think about into '22. Obviously, you have the Cordis proceeds that are coming in at \$1 billion, I believe. The tax receivable agreement, if I recall, is about \$1 billion or so, and I can double check that in the last quarter's transcript. When you think about that, think about your cash position as you sit now and the free cash that you're going to generate this year, even with the investments that you're making, do you think there's an opportunity to be a bit more aggressive, either on the buyback given where your stock sits in the market? On M&A, given that you talked about a number of growth priorities of which, I assume with some bolt-on transactions. Just curious about that philosophy where you sit now given that the company is in a stronger balance sheet position, as I can recall seeing in a while?

Mike Kaufmann: Thanks, Mike. I appreciate the question. And we are really excited about the work we've done around that. But I'm going to have Jason give you a little bit more color on it.

Jason Hollar: Yes. Thanks, Mike. And first of all, yes, I think we had some really great cash flow this last year. So \$2.4 billion of operating cash flow and that resulted in a \$3.4 billion ending cash balance, which does include the \$500 million debt paydown that we completed in the fourth quarter. So as you indicated perfectly, we are stepping into this year with a lot of flexibility even before the Cordis transaction closed, which was just a few days ago, which does add another \$1 billion to that balance.

As we highlighted in some of those comments this morning, we do expect to paydown the \$850 million that is coming due by the end of the fiscal year or before end of the fiscal year. So that will be one of those uses. And then, of course, we guided towards the \$500 million to \$1 billion for the share repurchases, which is a fairly wide range reflective of some of the flexibility that we talked about.

And as I think about the Cordis proceeds, of course, cash is somewhat fungible. But essentially, that \$1 billion, how we're thinking about it is accelerating some of that debt paydown and a portion of that, \$500 million to \$1 billion. So we feel real good about that as we entered into the first quarter here. You referenced the tax receivable. And I don't think we provided any updated comments on that so far.

Last quarter, I referenced that we expected by the end of the calendar year. That's still our expectation, like, I think, a lot of different organizations throughout the world right now. I think COVID has impacted some of the processes and a little bit less certainty as to the precise timing. But we still feel pretty good that's a good approximate time frame. But when you think about receiving those proceeds perhaps late in the calendar year, there will be less time to actually deploy those to the balance of this year. So that's certainly still a potential opportunity to get us maybe to some of the higher ends of that range. But nonetheless, there's a lot of flexibility that goes along with that.

As you indicated, when we talk about the opportunistic uses, essentially, we have increased flexibility here. M&A is always on that list. And it depends on the opportunity, the valuation and what we see is delivering to us strategically. And so that will be another thing that we evaluate along the year. Thanks for the question.

Operator: Up next, we'll hear from Kevin Caliendo with UBS. Please go ahead.

Kevin Caliendo: Great, thanks. I just want to expand on that a little bit. I guess I don't understand why you're not being more aggressive with the buybacks. Given the settlement looks like its largely done, the cash on hand is greater. The stock is going to come under pretty meaningful pressure today, most likely. What's stopping you from going out and buying \$2 billion of stock or more. Are there any credit issues or anything else that you're concerned about? And also, on the buyback, if I'm doing the math right, it feels like your -- like the numbers don't entirely jive to get to that \$0.21. Is there -- is it just simply the timing that it would happen so late in the year? Is why the buybacks wouldn't be covering the sort of \$0.21 of dilution from Cordis?

Mike Kaufmann: Yes. Let me start, Kevin, and then I'll turn it back over to Jason. I'll just comment specifically on the opioid piece and then let Jason give you a little bit more information. The opioid, as we said, we're pleased to get to the point where we are right now, where we have a comprehensive settlement out there. But it does have a few more steps left in it. So we do have to wait and see if we get the states and cities and counties to sign on to get enough critical mass in



order to make a final decision. And so we do have some time left on that to make sure that we understand exactly with clarity where that's going to be. But we're pleased with where we are as far as an initial step of finally getting something out there for people to consider.

And then let me now turn it over to Jason to go into a little bit more of the other details that you asked about.

Jason Hollar: Yes. And as it relates to the dilution on Cordis that was implied, a reference within there, it's just a matter of the timing of what you assume when we pay down the debt and when we would complete the share repurchases. And so there's an opportunity for that to have a reasonable range. And that guidance range, we think, reflects what we think that possibility may be -- but the key thing on a pro forma basis is that extra \$1 billion will be deployed in some manner. And we will see -- and certainly, within fiscal '23 run rate, there will not be dilution expected for that divestiture.

As it relates to your other question, as it relates to credit issues. There's nothing there. I mean we're on a gliding path to getting to our targeted leverage ratio. A key part that I referenced last quarter is that this remaining debt that's coming due at the end of this fiscal year is a key part of getting us towards those targets. And I indicated last quarter that I would anticipate the level of debt paydown to begin to diminish after this fiscal year. That continues to be our expectation. There's a lot of factors, as Mike just referenced, that could play into that.

But overall, that remains our viewpoint, and there's nothing here that is, I'll say, overly constructive from that point, just a little bit of prudence until we get some of these risks and uncertainties defined. And we also need to see underlying performance and cash flow over the course of the year. And then as I mentioned before, we do have some additional flexibility as it relates to the precise timing of the tax receivable.

Operator: And up next, we will take a question from Jailendra Singh with Credit Suisse. Please go ahead.

Jailendra Singh: Thank you and good morning, everyone. I want to go back to your this inventory impact on PPE in the quarter. Can you elaborate a little bit more on what products this relates to? And is there a potential that you might have another write-down in fiscal '22? And what kind of initiatives you're putting in place to ensure that this does not happen again?

Jason Hollar: Sure. Yes. So I'll go and start it. And -- so as Mike mentioned, the key thing here is that there's a lot of uncertainties with the pandemic. And we were, first and foremost, going to put our customer commitments in front of us, and that resulted in a higher level of inventory that we carried over that period of time. And that happened while there was obviously increasing demand, higher prices and lower -- longer than normal types of supply chains.

And then we step back -- every quarter, we would step back and do our analysis and determine what the net realizable value that is and then make any adjustments that may be necessary. So as Mike highlighted, there were some highly commoditized products. So it's a subset of our PPE that -- think of it as those products that would have more volatile type of pricing. We saw that move more dramatically over the period. And given it was a subset of our inventory, it was relatively defined. It was a relatively large percentage reduction within that, but it was contained to a certain subset.

And again, we're not going to get into all the details product-by-product, but it was that type of product that has a little bit less of the value add and then therefore, has a little bit easier to get more supply into the market and that drove the prices down quicker than other products. Anything else to add, Mike?

Mike Kaufmann: Only I'd reiterate that our focus has always been and will continue to be on our customer, and it was important to us from the very beginning of this pandemic to acquire critical PPE for our customers. And as Jason said, we did ramp up during a period of higher demand and higher prices and longer supply chains.

Operator: Next, we will hear from Ricky Goldwasser from Morgan Stanley. Please go ahead.

Ricky Goldwasser: Yes, hi, good morning. And thanks for all the details you provided in your prepared remarks. Just a couple of follow-up questions to understand sort of the moving parts in the guidance. So specifically, you talked about the customer renewal. It seems like it's CVS. Can you maybe help us quantify what the impact is in 2022? And also if there are any other renewals that we should be considering in the next 12 to 18 months? And then the second question towards at the moving parts are on the investment that you're making? Should we think about them as sort of a onetime investment in 2022? Or should we now factor just kind of like ongoing levels of investments to support future growth?

Mike Kaufmann: Yes, I'll start talk about the renewals and then I'll have Jason make a comment on the investments. The renewal that we're talking about had the -- Red Oak renewal is not at all included in what Jason was talking about on customer renewals. That's considered in our overall generics program performance, which we expect to be in -- to be something that we would expect to be a tailwind next year, and we feel really good about where we're headed with all the various components of our generics program and excited to continue to partner with CVS, moving forward with on Red Oak.

What Jason was talking about in renewals was just the normal renewals. There was nothing unexpected in the fourth quarter customer renewals. They basically came in as planned. And so that was not anything unexpected. I would consider it, as we look forward, we don't see customer renewals being any different or unusual for us in FY '22.

Jason Hollar: Yes. As it relates to the other moving pieces for Pharma, that are a part of that underlying guidance. Our growth business, as we expect to contribute. As Mike mentioned, we expect double-digit growth for our growth businesses, top line as well as bottom line. And for the Pharma business, that would be, of course, Specialty, Nuclear and Outcomes. And then we have the year-over-year COVID benefit that I mentioned would be a key part of that. But as Mike mentioned, that the customer renewals is not something that we would anticipate to be significantly different year-over-year.

And then your question regarding investments. Those investments are a mixture of -- we've spent quite heavily over the last couple of several years on the capital side of getting these IT systems in place. We are finalizing that multiyear journey now and are starting to depreciate those assets. So there will be elevated depreciation that, of course, is more fixed in nature. But there's also a component of the final testing and rollout launch of these systems tend to be more expense versus

capital. And so as we're right in that rollout stage, that expense will be elevated in that part, we would expect to reduce longer term, certainly beyond fiscal '22. But for the balance of this year, we would expect it to be elevated. And then thereafter, some portion of it will come down later on. Next question.

Operator: And up next, we'll hear from Eric Percher from Nephron Research. Please go ahead.

Eric Percher: Thank you. I wanted to ask about the generic volume commentary around certain classes. I know that we saw a clear increase in acute volumes from March into April and the quarter. So what are the classes where you're seeing this? And any other specifics on how that's impacting the generic program?

Mike Kaufmann: Yes. Thanks for the question. So a couple of things on that. We did see some sequential growth from Q3 to Q4 on generic volumes. So that continues to be a positive sign. We do expect our -- impact from COVID-19 on all generic volumes to be back at pre-COVID levels by the end of the calendar year or by the end of our Q2. What we're referring to here is we're still seeing, again, ramping up, but we're still seeing some less than pre-COVID volumes on areas like anti-infectives, antibacterials, antibiotics, antivirals and some pain medications that we've not seen.

Our thoughts are as life continues to get more and more back to normal, if that's the right word, kids are back in school, et cetera, we would start to see those drugs being needed more than they probably have historically been needed. So again, expect them to be back to pre-COVID levels by the end of the year, but that's really what we're talking about. Very similar to the exact same thing, we talked about last quarter, and it's kind of continuing to play out as we mentioned back then.

Kevin Moran: Next question, please.

Operator: And next, we'll hear from Steven Valiquette with Barclays. Please go ahead.

Steven Valiquette: ((Inaudible)) cost categories that are trending above baseline. So I'm curious if you're seeing those same trends as well?

Mike Kaufmann: I'm sorry, we didn't catch the beginning of your question. So if you could try it again. Thank you.

Steven Valiquette: Yes. Sorry, I knew at some point it would happen, I would be pinged to ask two questions on two calls at the same time, that just happens. So I guess I'm curious to if you could provide more color on the elevated supply chain cost you mentioned for the Medical segment in fiscal 4Q? You cited that in the press release. I guess I'm curious, geographically, is this cost pressure mainly in the U.S. or is it international as well, in addition to some other color just on mechanically what's happening there? And does the sale of Cordis alleviate this in any way into fiscal '22?

Mike Kaufmann: I'll start with your second piece first. Really, I don't see Cordis alleviating that at least towards the at least with the guidance we set. Of course, there could have been elevated costs on some of their raw materials and products. And Cordis being more international, obviously, it had more FX potential fluctuation. But don't see Cordis being a factor there.

As far as the elevated supply chain cost, what we started seeing in the fourth quarter is, I think, which you're hearing a lot of companies talking about, we're seeing increased fuel costs, we're starting to

see the cost of, for instance, containers can be 3 to 10x what they cost to ship in prior to COVID just due to ports being plugged, things like that.

So we're just -- wages, et cetera. So it's just those types of things that we're seeing general elevated supply chain costs across the board. Again, we saw that in Q4. We expect that to continue in for the first couple of quarters. And then as things get back to more normal, we'll be able to see some either reductions in those or we'll be able to take some of those costs and where possible that appropriately pass it through to customers if it's a more permanent type of thing. So we'll be monitoring that and keeping our eyes on that.

Operator: All right. And our next question will come from Elizabeth Anderson with Evercore ISI. Please go ahead.

(Eduardo): Hi, good morning. This is (Eduardo) on for Elizabeth. Can you guys maybe provide some more color on the \$250 million of additional cost savings opportunities? And I guess what areas of the enterprise you expect to generate those savings from?

Jason Hollar: Sure. Yes, I would say it's very much a continuation of what we've done to date. As you certainly recall, our initial target was the \$500 million, and we've come close to accomplishing that after the -- just the first three years. And that was in varied areas, everywhere from manufacturing, our footprint work there to our distribution work, all the way up to our functional areas. As we go forward, what we're seeing in this next stage is the ability to go from more of the transactional first order benefits like rate negotiation in areas like transportation and going further into really redesigning networks and getting into more augmented intelligence and things of that nature.

We have -- one area that is allowing us to unlock additional value in this next stage is the Cordis divestiture. We talked about the simplification of our international operating structure. That's an enabler for us to continue to go after additional opportunities there, and then just continue on at all fronts given that we've got good momentum in place already for the existing initiatives.

Mike Kaufmann: The only thing I would add is that, just to emphasize something Jason mentioned is around the use of digital to really get after being able to use bots, AI, RPA, et cetera, to get after our cost structure. We've been investing a lot of time on that. Our IT team has done a nice job of building out both people, resources and our businesses and functions are all embracing this as well as making sure we're doing work in the right locations are all in other important factors that we see being able to give us some tailwinds going forward on cost savings.

Kevin Moran: Next question, please.

Operator: All right. And up next, we'll hear from Lisa Gill with JPMorgan. Please go ahead.

Lisa Gill: Hi, thanks so much. Good morning. I just really want to understand as we think about normalization in your Pharma segment, so beyond the renewal, do you see low single-digit to mid-single-digit normalization in Pharma segment profit growth over the longer term? And where are specific opportunities that you see to maybe further accelerate that growth beyond 2022? That would be kind of my first question. And do things like Specialty and Nuclear that you talk about returning to double digit, I know they're on the smaller side, do they help to accelerate that low single-digit to mid-single-digit normalization? Just any drivers or help you can give around that on a longer-term basis.

Mike Kaufmann: Yes. Thanks, Lisa. Appreciate it. Actually, you hit a lot of it right there in your question, is that we did want to provide a normalized growth so that we could share with you what we do believe on our achievable longer-term growth rates for both of the businesses that we provided, the normalized growth on -- specifically, the Pharma, I think you said it well. We do expect continued double-digit growth from Nuclear and Specialty and our Outcomes businesses. We see all of them next year being able to grow top and bottom lines by double digits. And we continue to see those businesses continue to be a bigger and bigger portion of the overall Pharma segment.

So as they continue to grow at those rates and are a bigger portion of the segment, obviously, they're going to continue to have more and more impact. We feel really good about the pipeline of products in Nuclear. And with the work we're doing in our center for advancement of Theranostics, we already have a significant amount of manufacturers committed to joining us in the center when we open it and working together on some new both treatments and diagnostics for cancer and other areas. So we feel good about all of those businesses.

And then as far as the core PD business goes, we think we are well positioned with some very large and important customers, that you're aware of. We've got eight more years now on our agreement related to Red Oak, and we feel good about that partnership and that's continued positive impact on our generics program. And so those are some of the things, I would say, make us feel good about that growth going forward.

Kevin Moran: Next question, please.

Operator: And next, we'll hear from George Hill with Deutsche Bank. Please go ahead.

George Hill: Hey, good morning, guys. And thanks for taking the questions. I guess Mike, first, I would ask you, with the renewal of the Red Oak agreement, are there any substantive changes to the economics of that agreement? And then number two, you guys called out contingent brand inflation in the press -- I'm sorry, in the presentation. As the business is starting to mix back towards brand growth, are you seeing any changes in the underlying economics of the brand relationships and the amount of profit that's exposed to brand price inflation?

Mike Kaufmann: Yes, two very good questions. So first of all, on brand. What we're seeing there is we're expecting the overall inflation rate to just be similar for the last couple of years. So we're not seeing any real changes there. And as Jason mentioned, the reason you said getting less dollars is because more of the suppliers that were contingent to inflation have moved to non-contingent, and we've renegotiated a couple of those DSAs over the last year so that we will no longer be contingent to inflation.

As far as overall rates go, I would say, we continue to feel very good about our overall value proposition. We have very strong relationships with manufacturers. And as you know, when any time there's changes in their portfolios, sometimes that means they should get a lower price when they have higher cost drugs coming out and sometimes they need to pay more fees when they lose, say, a high-priced item to a patent expiration. And so those types of moving parts in terms of volume and average line extension are taken into account with each negotiation, and the team has done an excellent job working with our manufacturing partners and continue to have what I consider to be a

fair market rate for that and feel very good about that, being able to be something that we can continue going forward.

As far as the Red Oak, we won't be able to get into any specifics there. But as you can imagine, it's been an excellent seven-year relationship. The team there continues to remain intact. They have decades of generic buying experience. The leadership there and the team has -- just a great group of individuals, again, with experience that continues to bring new ideas together to the market to be able to help us continue to get the best cost in the marketplace. And we continue to partner well with CVS at Board meetings, et cetera, to continue to drive that.

So we feel that the -- both companies took into -- in the context all the market conditions on generics when we renegotiate. We feel very good about where we are with our Red Oak extension.

We'll take one last question.

Operator: And our last question will come from Charles Rhyee from Cowen. Please go ahead.

Charles Rhyee: Yes. Thanks -- thanks for squeezing me in here. Maybe, Mike -- maybe a question on opioids and the settlement here. I think there's like 150 days or so that -- for the plaintiffs to accept the terms of the settlement. What's the minimum participation that's required under this settlement for it to go into effect? So in other words, is it like half the participants have to at least participate? And then it's my understanding that the amount that you would pay out would scale down depending on the number of participants. So I just wondered what that minimum requirement is? And what happens if you don't hit that threshold? Thanks.

Mike Kaufmann: Yes. Thanks for the question. So you're right. So the total number that is accrued assumes all 50 state, cities and counties are in. So if any single state or cities and counties within states do not elect to be part of it, the number will come down based on agreed upon proration by state. So it will decline at states not -- and cities and counties do not participate.

Second thing, to your point, it is multi-steps. There's a point where we get some insights to where the states are. Then there'll be another point where we'll get to understand where the cities and counties and the subdivisions are. And after all of that, we will take a look at what we call -- we're calling critical mass. There is no set number. So there's no minimum.

Our goal has been and continues to be to get 100% participation on all 50 states in order to have the most clarity. That may not happen and anything less than that. And we, as a group, we'll have to sit down and determine if that's enough clarity and participation. It's highly dependent on the states that do and don't participate. So we'll have to really step back and look at it as an overall -- from an overall standpoint and make a decision on whether or not to move forward.

Jason Hollar: One thing I'd like to just clarify, as Mike indicated, if not all 50 states choose or we from an arrangement to join, that would mean the cash payments would be lower under that structure. It does not necessarily mean the accrual changes. And that would -- we look at the facts and circumstances of the situation to determine what the proper accounting would be at that time. So there could certainly be a difference there that we would need to evaluate.

Mike Kaufmann: Good clarification.

Operator: And that concludes our Q&A session for today. I will now turn the conference back to Mike Kaufmann for his closing remarks.

Mike Kaufmann: Yes, I want to thank everybody for taking the time to be on the call and for the very helpful questions. I know there was a lot of noise in this quarter, but I just want to end with a few thoughts to keep in mind. We did see -- first, we did see underlying growth in FY '21 in both of our segments, if you exclude COVID-19, which gives us confidence as we move forward -- going forward with the impacts of the pandemic hopefully beginning to dissipate.

Our guidance is for growth next year in each segment. And then also if you take normalized growth in each segment, when you normalize for noise like COVID and Cordis divestiture, we will grow in both segments. We have tailwinds behind our growth businesses. We really expect all of our growth businesses as a group to really grow at least double digits on the top and bottom line. And we have taken some significant actions such as getting after an additional \$250 million in cost savings; closing the Cordis transaction, which will enable us to simplify our operating model; and extending our agreement with CVS are just a few of the examples. And as the first question was in Jason's comment, we do have very strong cash flow generation, which gives us a lot of flexibility to be more opportunistic in our capital deployment.

So with that, thanks again, and have a good day.

Operator: And this concludes today's call. We thank you for your participation. You may now disconnect.