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# McKesson Corp. (MCK)

## Q3 2023 Earnings Call

# CORPORATE PARTICIPANTS

**Rachel Rodriguez**
*Investor Relations Contact, McKesson Corp.*

**Brian S. Tyler**
*Chief Executive Officer & Director, McKesson Corp.*

**Britt Vitalone**
*Chief Financial Officer & Executive Vice President, McKesson Corp.*

# OTHER PARTICIPANTS

**Michael Cherny**
*Analyst, BofA Securities, Inc.*

**Lisa C. Gill**
*Analyst, JPMorgan Securities LLC*

**Eric Percher**
*Analyst, Nephron Research LLC*

**Charles Rhyee**
*Analyst, Cowen & Co. LLC*

**George Hill**
*Analyst, Deutsche Bank Securities, Inc.*

**Steven Valiquette**
*Analyst, Barclays Capital, Inc.*

**Brian Tanquilut**
*Analyst, Jefferies LLC*

**A. J. Rice**
*Analyst, Credit Suisse Securities (USA) LLC*

# MANAGEMENT DISCUSSION SECTION

**Operator**: Welcome to McKesson's Third Quarter Fiscal 2023 Earnings Conference Call. Please be advised that today's conference is being recorded.

At this time, I would like to turn the call over to Rachel Rodriguez, VP of Investor Relations. Please go ahead.

## Rachel Rodriguez
*Investor Relations Contact, McKesson Corp.*

Thank you, operator. Good afternoon, and welcome, everyone, to McKesson's third quarter fiscal 2023 earnings call. Today, I'm joined by Brian Tyler, our Chief Executive Officer; and Britt Vitalone, our Chief Financial Officer. Brian will lead off, followed by Britt, and then we will move to a question-and-answer session.

Today's discussion will include forward-looking statements such as forecasts about McKesson's operations and future results. Please refer to the cautionary statements in today's earnings release and presentation slides available on our website at investor.mckesson.com and to the Risk Factors section of our periodic SEC filings for additional information concerning risk factors that could cause our actual results to materially differ from those in our forward-looking statements.

Information about non-GAAP financial measures that we will discuss during this webcast, including a reconciliation of those measures to GAAP results can be found in today's earnings release and presentation slides. The presentation slides also include a summary of our results for the quarter and updated guidance assumptions.

With that, let me turn it over to Brian.

## Brian S. Tyler

*Chief Executive Officer & Director, McKesson Corp.*

Thank you, Rachel, and thanks, everyone, for joining us on our call this afternoon. Today, we reported third quarter fiscal 2023 results, another quarter with solid Adjusted Operating Profit growth, underscoring the significant progress we continue to make in our company in terms of our overall company priorities. It also signals the continued strength and stability of our North American businesses. As a result of our third quarter performance and business outlook, we are raising our guidance range for fiscal 2023 Adjusted Earnings per Diluted Share from $24.45 to $24.95 to an updated range of $25.75 to $26.15.

During today's call, I'm going to highlight the progress we've made across our four strategic priorities. Then I'll ask Britt to provide additional details on the financial performance in our third quarter. As you know, a few years ago, we crafted our enterprise strategy and we shared our priorities with our stakeholders. We are evolving our portfolio of capabilities, and we have divested businesses that are not aligned with our strategy. And we have invested both organically and through acquisitions to add to our differentiated capabilities.

We're increasing our focus on the areas where we have deep expertise and that are central to our long-term growth strategy. Our progress to date is underpinned by the execution against these important company priorities: a focus on people and culture; intentional efforts to evolve and grow our portfolio of capabilities; to advance and expand our differentiated oncology ecosystem and our biopharma services platform; and our commitment towards sustainable core growth. The strength of our core distribution businesses continued to show solid growth and generate Free Cash Flow, which provides us a strong balance sheet and the ability to invest internally and externally into the business.

I'll start with our first priority, our focus on people and culture. Embedded in our daily operations is our purpose, advancing health outcomes for all. McKesson is an impact-driven organization. We recognize that giving back to the community is important to our associates, and we continue to provide engaging and, most importantly, impactful ways for Team McKesson to do exactly that. In the third quarter, we had another successful Community Impact Day, where nearly 13,000 members of Team McKesson across North America volunteered to support nonprofits that provide food to people facing hunger.

McKesson also held its annual Giving Tuesday, where Team McKesson's generosity resulted in $1.5 million in employee donations, with a portion of that matched by the McKesson Foundation, which will ultimately be distributed to 1,500 local, national and global charities. In addition to the progress made by our employees, the McKesson Foundation donated more than $4 million to pharmacy schools to help increase workforce diversity and improve overall health outcomes for vulnerable populations. These grants, which range from one to five years in duration, will support various pharmacy school education and community outreach programs.

The innovative student support, professional development and community outreach that the McKesson Foundation is funding through these pharmacy school partnerships will help transform patient-pharmacist interactions, which we believe will lead to improved health equity and patient outcomes for vulnerable populations in their respective areas. I'm proud of our talented team as their dedication, hard work and innovation enables our business to positively impact our partners, our customers and our communities.

Our next priority is to evolve and grow the portfolio. We have continued to evolve and grow our capabilities, ensuring that our capital deployment is tightly aligned with where we have the best growth opportunities. This led us to our decision to exit the European region as well as a handful of smaller businesses over the last several years. We're progressing on our plans to exit the European region and have successfully exited 11 of the 12 countries we operated in. We remain committed to exploring strategic alternatives for our business in Norway, which is the only country we have not yet divested. These actions allow us to focus our resources on areas that support our long-term strategy. It's provided us additional flexibility to invest internally or to look externally to expand our oncology and our biopharma ecosystems, which aligns well with our next company priority.

We have made meaningful progress expanding our oncology and biopharma ecosystems as exemplified by the strategic investments made year-to-date. McKesson recently announced that The US Oncology Network, the US's largest oncology practice management organization, has continued to expand its geographic footprint with the addition of two new practices, Epic Care in California and Nexus Health in New Mexico. Both are now part of The US Oncology Network as of January 1, 2023. These practices offer a wide range of specialties, enabling more comprehensive care that helps ensure patients can conveniently receive the care they need in their local communities during their entire treatment and healing journey.

And we're excited by the new opportunities that our joint venture with Sarah Cannon Research Institute as well as the acquisition of Genospace bring to our overall oncology ecosystem. I'm pleased with the substantial progress we've made in the development and expansion of our oncology ecosystem. This progress supports the solid performance of the US Pharmaceutical segment as we further our long-term growth strategies. We will continue to evaluate internal and external opportunities to invest, to grow and to evolve this business.

In addition to our oncology assets and capabilities, our biopharma services platform remains another priority area of growth. Over the last several years, we've systematically built and acquired an ecosystem of assets that complement on each – that complement each other and are more valuable together than as separate stand-alone solutions. Together, these assets leverage our network reach, technology and clinical expertise to enable better access and affordability of medications, which ultimately improves patient outcomes and impacts real lives.

We started building this business in 2006 with the acquisition of RelayHealth, which gave us connectivity to over 50,000 pharmacies. We've been able to integrate value-added services right into the workflow so that we can help their processes be more seamless and give the customer the experience they need and deserve. We then acquired CoverMyMeds, a long-term partner of McKesson in 2017. This expanded our network by providing connectivity with over 750,000 providers. The integration of CoverMyMeds' automation solution alleviates some of the friction out of the workflow providers, improving overall access for the patient.

RxCrossroads brought a scale in the business that we already had, a hub services and patient support program, and they expanded our clinical expertise across many new therapeutic areas. In 2020, recall, we brought these businesses together as Prescription Technology Solutions so we can migrate from providing individual offerings to a more comprehensive end-to-end suite of solutions. This enabled us to enhance our value proposition and to help find and get patients started on appropriate therapy more quickly.

Most recently, we acquired Rx Savings Solutions, which helps employers and health plans reduce prescription drug costs by utilizing its advanced analytics capabilities. It's more than just price transparency. It really gives members insight and actionable guidance that can drive savings and improve health outcomes for patients. So by bringing these businesses together, Relay, CoverMyMeds, RxCrossroads, Rx Savings Solutions, our McKesson Prescription Technology Solutions connect pharmacies, providers, payers and biopharma manufacturers for really next-generation patient access, affordability, and adherence solutions that are automated and integrated into provider workflows.

CoverMyMeds now processes approximately 21 billion pharmacy transactions annually on behalf of patients to support medication access and affordability. We continue to build and invest in innovative products that allow McKesson to provide unique insights and capabilities to our customers. And these investment dollars are reflected in our results in the segment year-to-date as well as in our fiscal 2023 outlook. During the third quarter, we continued to organically invest in this segment as we position our products and services for sustainable long-term growth. The investments have enabled us to expand the network and connectivity, develop new solutions and meet the growing demands of our customers.

While we continue to invest and grow the platform, we're also always assessing opportunities to evolve and streamline the portfolio to ensure our resources and investments are focused on the products that bring the most value to patients. This business saw substantial momentum coming out of COVID-19 pandemic as our biopharma manufacturers continued to bring more brands to our platform and prescription utilization trends continued to improve. These factors led to strong Adjusted Operating Profit growth in this segment in recent fiscal years. We remain confident in the overall trajectory in this segment and our financial target of 11% growth. And we will continue to reinvest profit into this business to accelerate this business over the long term.

The investments made in our oncology and biopharma ecosystems have been possible largely due to the long-standing growth in our sustainable core distribution businesses, which are our fourth company priority. As we exit the European region, we've been able to focus our efforts on our North American businesses. Our teams are continuously evaluating how to drive efficiencies in our core operations. Whether that's leveraging a more modernized platform, it allows us to act with more speed and agility or ensuring we have the optimal talent and resources to help these businesses succeed.

The fundamentals of our US Pharmaceutical and Medical-Surgical Solutions segment remains strong. The work that Team McKesson has done to streamline process and efficiencies, combined with positive prescription volume and patient utilization trends, reinforces our confidence in our long-term growth for our North American distribution businesses.

In the US Pharmaceutical business, I'm excited to announce that our contract to extend our pharmaceutical distribution partnership with CVS Health through June of 2027 has been finalized. Our long-standing partnership with CVS further exemplifies the value of our scaled distribution capabilities.

The performance of the core operations in our North American distribution business enables strong cash flow generation that's allowed McKesson to continue to innovate and become a leading diversified healthcare services company. We believe we've made significant strides against our strategic priorities to focus on our people and culture, to grow and evolve the business, to invest in our oncology and biopharma services ecosystem underpinned by the sustainable core growth in our distribution businesses.

Let me shift gears just a bit. McKesson has also made progress recently to address environmental sustainability. In January, McKesson received approval by the Science Based Targets initiative for its near-term climate change targets that contribute to reducing its greenhouse gas emissions. Our SBTi target serve as another example of our commitment to sustainability and our response to climate change.

We look forward to leveraging the advancements in climate-related technologies that will address these environmental challenges while also enhancing our business and helping to fulfill our company purpose of advancing health outcomes for all. We will, of course, continue to provide updates on our progress to stakeholders on these targets as well as our ongoing ESG-related initiatives on future calls.

As an organization, we're also committed to advancing diversity, equity and inclusion. McKesson was recently recognized by Newsweek as one of America's Greatest Workplaces for Diversity in 2023. We're quite honored that Newsweek recognizes McKesson's ongoing efforts to be a more diverse and inclusive employer.

All right, let me wrap things up. We are pleased with our solid results in the third quarter as we delivered on our growth strategy and as a diversified healthcare services company. McKesson's talented employees continue to demonstrate exceptional performance, and our third quarter results reflect their dedication and our execution together as a team in a dynamic operating environment. It also highlights the resiliency of our portfolio of businesses and solutions.

Thank you all for your time. With that, Britt, I'm going to toss it over to you for additional comments on the financial results.

## Britt Vitalone

*Chief Financial Officer & Executive Vice President, McKesson Corp.*

Well, thank you, Brian, and good afternoon, everyone. Our solid fiscal third quarter financial results reflect continued strong execution and momentum, advancing our company priorities.

In the fiscal third quarter, we delivered solid growth across our North American segment, led by strong performance in the US Pharmaceutical and Medical-Surgical Solutions segments. And we continue to evolve and grow our diversified portfolio through focused and strategic investments in oncology and biopharma services. As a result of our solid financial performance and confidence in the underlying business, we are increasing and narrowing our full year outlook for fiscal 2023 Adjusted Earnings per Diluted Share to a range of $25.75 to $26.15.

Before I provide more details on our third quarter fiscal 2023 non-GAAP adjusted results, I want to point out two items that impacted our GAAP-only results in the quarter. First, we received proceeds of $129 million related to our share of an antitrust class action settlement. We recognized the gain within cost of sales in the third quarter. And second, we recognized a pre-tax gain of $97 million from the termination of fixed interest rate swaps. This gain is included under other income in the third quarter.

Let's move now to a review of our third quarter non-GAAP adjusted results on a year-over-year basis. Consolidated revenues of $70.5 billion increased 3%, driven by growth in the US Pharmaceutical segment resulted from increased specialty product volumes, including retail national account customers, partially offset by lower revenues in the International segment, resulting from the completed divestitures of McKesson's European businesses. Excluding the impact of our European business operations, including completed divestitures, revenues increased 11%.

Gross profit was $3 billion for the quarter, a decrease of 10%. Excluding the impact of our European business operations and completed divestitures, gross profit increased 7%, primarily a result of growth in the US Pharmaceutical segment. Operating expenses in the quarter decreased 14%, largely driven by completed European divestitures in the International segment. Excluding the impact of our European business operations, including the completed divestitures, operating expenses increased 9%.

Operating profit was $1.4 billion, an increase of 9%, driven by a pre-tax benefit of $126 million related to the early termination of the tax receivable agreement, or TRA, with Change Healthcare and due to growth across North American businesses led by the strong performance in the US Pharmaceutical segment.

As a reminder, McKesson was a party to a TRA entered as part of the formation of the joint venture with Change Healthcare. Under the terms of the TRA, Change was generally required to pay McKesson a portion of net tax savings resulting from amortization by the joint venture. In October of 2022, Change exercised its right to terminate the agreement and paid McKesson $126 million. Consistent with our prior practice recognizing similar items, this benefit is reflected in other income in both our GAAP and adjusted operating results in the quarter.

Moving below the line, interest expense increased to $69 million in the quarter, primarily due to higher interest rates and unfavorable impacts in our derivative portfolio as we exit the European region. And the effective tax rate was 23.4% for the quarter. As a reminder, our effective tax rate can vary quarter-to-quarter, driven by our mix of income and the timing of discrete tax items. For the full year, we continue to expect an adjusted effective tax rate in the range of 18% to 20%.

Wrapping up our consolidated results. Third quarter diluted weighted-average shares outstanding was approximately 141 million, a decrease of 8%, resulting from share repurchase activity. Overall, third quarter Adjusted Earnings per Diluted Share was $6.90, an increase of 12% compared to the prior year. When excluding the impacts from COVID-19-related items and the benefit from the early termination of the tax receivable agreement with Change, Adjusted Earnings per Diluted Share increased 6%.

Moving now to our third quarter segment results, which can be found on slides 7 through 12 and starting with US Pharmaceutical, where revenues were $61.9 billion, an increase of 13% year-over-year, resulting from increased volume of specialty products, including higher volumes from retail national account customers, branded pharmaceutical price increases and strength in oncology, which included increased patient visits, partially offset by branded to generic conversions. Operating profit increased 6% to $778 million.

Our contract with US government for COVID-19 vaccine distribution provided a benefit of approximately $0.25 per share in the quarter compared to $0.26 per share in the third quarter of fiscal 2022. When excluding the impact of COVID-19 vaccine distribution, US Pharmaceutical segment delivered operating profit growth of 7%, driven by growth in distribution of specialty products to providers and health systems, contributions from our generics programs, and improvements in pharmaceutical prescription volumes and oncology visits.

In the Prescription Technology Solutions segment, revenues were $1.1 billion, an increase of 9% year-over-year, driven by increased prescription volumes, faster growth in our third-party logistics business and higher technology service revenues. Operating profit increased 7% to $155 million, driven by growth in access, affordability, and adherence solutions, partially offset by continued organic investments as we position our products and services for sustainable long-term growth.

Next, moving on to Medical-Surgical Solutions. Revenues were $3 billion, a decrease of 3%. Lower volumes of COVID-19 tests and kitting, storage, and distribution of ancillary supplies for the US government's COVID-19 vaccine program partially offset the growth in the primary care business. Operating profit increased 2% to $336 million. The contribution from COVID-19 tests and our contract with the US government for the kitting, storage, and distribution of ancillary supplies provided a total benefit of approximately $0.38 per share in the quarter as compared to $0.57 per share in the third quarter of fiscal 2022.

Excluding the impact of COVID-related items, the Medical-Surgical Solutions segment delivered operating profit growth of 25%, driven by growth in the primary care business and favorable sourcing activities, which partially offset lower volumes of the COVID-19 tests and lower contribution from kitting, storage, and distribution of ancillary supplies from the US government's COVID-19 vaccine program.

Next, let me address our International results. Revenues were $4.4 billion, and operating profit was $143 million, a decrease of 36%. On an FX-Adjusted basis, revenues were $4.9 billion, a decrease of 48%, and operating profit was $158 million, a decrease of 29%. Third quarter results reflect the year-over-year effect from the divestiture of the European businesses.

Moving next to corporate. Corporate expenses were $19 million, a decrease of 88% year-over-year, driven by the early termination of the tax receivable agreement with Change Healthcare and lower opioid-related litigation expenses. Excluding the benefit from the early termination of the tax receivable agreement, corporate expenses decreased 9%. Additionally, we incurred opioid-related litigation expenses of $9 million in the third quarter, and we anticipate that fiscal 2023 opioid-related litigation expenses will be approximately $50 million.

Turning now to our cash position, which can be found on slide 13. As a reminder, our cash position, working capital metrics and resulting cash flows can each be impacted by timing and vary from quarter-to-quarter. We ended the quarter with $2.8 billion in cash and cash equivalents. During the first nine months of the fiscal year, we made $376 million of capital expenditures, which includes investments in distribution center capacity, automation and regulatory enhancements and investments in technology, data and analytics to support our growth priorities, including our oncology and biopharma services ecosystems.

For the first nine months of fiscal 2023 and 2022, we had Free Cash Flow of $1.5 billion and $1.2 billion, respectively. During the quarter, we allocated $833 million towards M&A activities, including a joint venture with the Sarah Cannon Research Institute and the acquisition of Rx Savings Solutions.

We also returned $2.1 billion to shareholders, including $2 billion of share repurchases. Year-to-date, we returned $3.7 billion of cash to shareholders, which included $3.5 billion of share repurchases and $216 million in dividend payments. At the end of our fiscal third quarter, we had $3.8 billion remaining on our share repurchase authorization.

Let me turn to our fiscal 2023 outlook. A full list of our assumptions can be found on slides 15 through 18 in our supplemental slide presentation. And I'll begin with our consolidated outlook. Our revised guidance assumes 3% to 7% revenue growth and 2% to 6% operating profit growth as compared to fiscal 2022.

Our guidance includes $2.30 to $2.50 of contribution attributable to the following four items: $0.70 to $0.80 related to the US government's vaccine distribution in our US Pharmaceutical segment; $1.10 to $1.20 related to COVID-19 tests and the kitting, storage, and distribution ancillary supplies in our Medical-Surgical Solutions segment; approximately $0.15 related to year-to-date net losses associated with McKesson Ventures' equity investments; and a $0.65 benefit related to the early termination of the tax receivable agreement with Change Healthcare. As a reminder, our contracts with the US government for the distribution of COVID-19 vaccines and the kitting, storage, and distribution of ancillary supplies extends through July of 2023.

We anticipate corporate expenses in the range of $435 million to $475 million, which includes net losses associated with McKesson Ventures' equity investments, which we recorded in the first three quarters of the fiscal year, and the benefit from the early termination of the tax receivable agreement with Change Healthcare, which was recognized in the third quarter. As a reminder, our practice has been and will continue to not include McKesson Ventures' portfolio estimates in our guidance.

When excluding the impacts from COVID-19-related items, net gains and losses associated with McKesson Ventures' equity investments and the benefit from the early termination of the tax receivable agreement with

Change Healthcare, we anticipate operating profit to increase 7% to 11%, above the previous operating profit growth target.

Moving below the line, we anticipate interest expense to be in the range of $245 million to $255 million. The increase compared to the prior guidance reflects the higher interest rate environment. Our anticipated full year effective tax rate of approximately 18% to 20% remains unchanged. Based on our third quarter results and our outlook for the fiscal year, we're increasing and narrowing our guidance range for Adjusted Earnings per share to $25.75 to $26.15 from the previous range of $24.45 to $24.95.

When excluding the impacts of COVID-19-related items, net gains and losses from McKesson Ventures' equity investments for both fiscal 2023 guidance and fiscal 2022 results and the fiscal 2023 benefit from the early termination of the tax receivable agreement with Change Healthcare, our Adjusted Earnings per Diluted Share guidance indicates approximately 13% to 16% growth over the prior year.

Moving now to the segment outlook for fiscal 2023. In the US Pharmaceutical segment, we anticipate reported revenue to increase 12% to 15% and operating profit to increase 5% to 8%. As I outlined earlier, our outlook includes approximately $0.70 to $0.80 related to COVID-19 vaccine distribution for the US government. When excluding the impact of COVID-19 vaccine distribution for the US government, we anticipate 7% to 9% operating profit growth. We are pleased with the momentum of the segment. Our pharmaceutical distribution business continues to deliver stable growth through focused execution and operational excellence.

Let me highlight a few of the factors that are leading to the strong segment performance. First, we've observed stable prescription utilization growth, which underpins the momentum in our health system and retail offerings. Second, we maintain a favorable outlook for our oncology platform, which we see delivering higher growth and higher margin contributions. We continue to execute and invest against our oncology strategy. And as Brian touched on earlier, we continue to add practices and providers to our scale and growing US Oncology Network, and we are well positioned to capture increased oncology volumes.

Third, we have a scaled an efficient generic sourcing operation, delivering stability of supply and low-cost products for our customers and patients. And specific to fiscal 2023, through the month of January, we observed branded pharmaceutical pricing that was modestly above our expectations. While fiscal 2023 results benefit from this modest increase, I would make the following two comments: first, the impact from higher branded pharmaceutical pricing remains less material now than historically, as more than 95% of our manufacture contracts are now on a fixed fee-for-service arrangement; and second, we would not anticipate this modest benefit to repeat in future years.

Our US Pharmaceutical segment is well positioned and has exhibited strong performance, leading to the increased fiscal 2023 growth outlook. As a result of our execution and the factors that I just noted, we anticipate that this segment will now grow above the 4% earnings growth target rate that we previously provided, including at our 2021 Investor Day.

The products and services within the Prescription Technology Solutions segment delivered differentiated access, adherence and affordability products. We are pleased with the solid growth in both revenue and operating profit this quarter. Biopharma services remain an important strategic growth and investment area for McKesson. We're confident this segment will exhibit faster growth and higher margin. We remain confident in our differentiated assets and capabilities. We have unmatched scale across transactions, provider and retail connectivity and product breadth.

Our commitment to this segment is evidenced by the investments that we have made. Over the past three years, on average, we've organically invested approximately $100 million a year into new and existing products and services. And our recent acquisition of Rx Savings Solutions will accelerate the breadth of capabilities we continue to build out.

We also anticipate further organic investments in new capabilities as well as more M&A. The internal investment pattern, the mix of technology products and third-party logistics services and the life cycle of the products we serve, including the timing of launches, have resulted in variability in performance quarter-to-quarter. As we continue to invest and grow the business, we anticipate that there could be charges to further integrate product portfolios and supporting infrastructure.

We anticipate delivering revenue growth of 10% to 16% and operating profit growth of 14% to 17%, which is in line with the 14% to 20% initial guidance that we've communicated on our May 2022 earnings call and above the operating profit growth target of 11% provided at our Investor Day event in 2021. We are well positioned for strong growth, and we're committed to the operating growth targets that we've previously communicated.

In the Medical-Surgical Solutions segment, we anticipate reported revenues to decrease 1% to 5% and operating profit to decrease 1% to 4%. As previously mentioned, our outlook includes approximately $1.10 to $1.20 related to COVID-19 tests and the kitting, storage, and distribution of ancillary supplies for the US government. Excluding the impact of COVID-19-related items, we anticipate Medical-Surgical operating profit to increase 12% to 15%.

Finally, in the International segment, we anticipate revenues to decline by 42% to 46% and operating profit to decline by 26% to 29%. This year-over-year decrease includes the loss of operating profit contribution from businesses and transactions that we have closed to date.

For fiscal 2023, we anticipate our European operations will contribute operating profit of approximately $0.90 to $0.95 per diluted share, primarily in the first nine months of the fiscal year. This includes year-to-date contributions from operations prior to completed sales, our operations in Norway and the contribution resulting for held-for-sale accounting for the transaction with the PHOENIX Group.

Let me conclude our outlook with a review of cash flow and capital deployment. We continue to anticipate Free Cash Flow of approximately $3.2 billion to $3.6 billion, which is net of property acquisitions and capitalized software expenses. In fiscal 2023, our cash flows have also been impacted by European divestiture activities and other transactions. As discussed last quarter, our Free Cash Flow guidance includes approximately $900 million of negative impacts from our European operations and divested assets.

We remain committed to be good stewards of capital for our shareholders. We have and will continue to take a disciplined approach to capital allocation. We strategically think about capital allocation in three broad categories. First, we prioritize growth by investing internally and through M&A. We are focused on accelerating our strategic growth pillars of oncology and biopharma services. These growth platforms have differentiated asset scale and network capabilities.

Next, we will continue to return capital to shareholders through a combination of our growing dividend and share repurchases. And the third piece of our framework is a strong balance sheet and adequate liquidity underpinned by the maintenance of investment grade credit rating. Our outlook continues to incorporate plans to repurchase approximately $3.5 billion of shares, which has been largely completed by the end of our fiscal third quarter. As a result of the share repurchase activity, we estimate weighted average diluted shares outstanding to be approximately $142 million.

Let me take a moment and reflect on the fiscal 2023 outlook and our growth targets. At our 2021 Investor Day event, we shared with you a set of growth metrics that reflect our commitment to drive continued momentum across the business segments. Since then, we've executed on our strategy and delivered operating profit growth consistently at or above the targets that we communicated on a consolidated and on a segment level.

Some of the business dynamics that we outlined previously have materialized as tailwinds and contributed to recent growth, including growth in prescription volume and patient mobility, our ability to grow through macroeconomic unpredictability and successful execution on a disciplined capital deployment strategy that focuses on growth and maximizing shareholder return. More importantly, the solid performance is further demonstration of our shareholder value creation framework. We continue to be focused on profitable growth and efficient deployment of capital. Our 24% return on invested capital illustrates our focus on shareholder value creation.

In closing, we are pleased with the results of our fiscal third quarter. We continued to deliver solid operating results through focused execution and strategic investment. Looking ahead, we're confident in our ability to deliver sustainable long-term growth. Our disciplined growth strategy and financial framework give us the confidence we will deliver on our operating profit growth targets.

Thank you. And now with that, I'll turn the call over to the operator for your questions.

# QUESTION AND ANSWER SECTION

**Operator**: Thank you. [Operator Instructions] And our first question comes from Michael Cherny with Bank of America.

**Michael Cherny**
*Analyst, BofA Securities, Inc.*

Q

Good afternoon. Thank you.

**Brian S. Tyler**
*Chief Executive Officer & Director, McKesson Corp.*

A

Hey, Mike.

**Michael Cherny**
*Analyst, BofA Securities, Inc.*

Q

Good afternoon. Thank you for taking the question. Hey, everyone. Diving into the Prescription Technology Solutions business a bit, I know it continues to evolve in terms of the assets that you've put in place, continued organic investment you make. As you think about the ability to continue on, sustain the pathway of your long-term growth targets, how much are you working on in terms of the dynamics of visibility within your own business, not just to the Street, but ensuring that on a quarter-by-quarter basis, some of the, I guess, I'd call it, lumpiness that we've seen in the last couple of quarters can smooth itself out. And how will this business evolve on that front in terms of that level of visibility and your ability to continue to convert successful sales, successful organic investment into the sustained long-term growth rate?

**Brian S. Tyler**
*Chief Executive Officer & Director, McKesson Corp.*
A

Great question. I'll maybe – let me kick it off first. I'd say we continue to be pleased with the performance of this business. I mean, we've got revenue growth of 9% year-over-year, AOP growth of 7% this year. Last two years have been particularly strong for this business. And what you find is as you continue to add capabilities into this business, we find opportunities for new ideas, new invention, reinvention, sometimes reprioritization of the projects. But we shared at Investor Day, we think this is a $15 billion-plus market opportunity in access, affordability and adherence. And we see a relatively long runway and we feel pretty confident in our 11% target growth for this segment. Now there are things that naturally happen in this business that may make it. I think your word was lumpy. Maybe that was our word. It became your word.

Things like the recovery pace of underlying prescription volumes. The commercial success of some of the projects we partner with, do they underachieve or overachieve their expectations, loss of exclusivity events. Our investments, I mean, we've made significant investments in this business over the last three years. We see continued opportunity to do that and that's not always completely smooth. I mean, the nature of those opportunities is going to be variable. Our process is to make sure that we've got disciplined line of sight, financial expectations and that those are prudent and good investments to make to sustain the growth in this segment long term.

**Britt Vitalone**
*Chief Financial Officer & Executive Vice President, McKesson Corp.*
A

And Mike, maybe what I would add is while we have seen a little bit of variability quarter-to-quarter, one of the things that is just inherent in this business and we talked about this is the annual customer verification process that we do for a lot of our customers, and that usually happens in the fourth quarter. What I would say, though, is that what we are pleased with, if you go back to the guidance that we gave you at the beginning of the year in May, 14% to 20%. The guidance that we're giving you now to finish the year is really within the balance of that guidance. It's been, as I said, a little bit of variable quarter-to-quarter, but it's really in line with the guidance that we gave at the beginning of the year.

And we're really pleased that while we've been investing in this business, both organically and through M&A, that we're seeing this business develop above the long-term target rates that we gave you at Investor Day. So while we've seen a little bit of – a little more variability this year quarter-to-quarter than we may have seen historically, when you look at it on an annual basis and you look at it over the long term, which is how we manage the business, we're seeing this above the long-term target rates that we gave and really in line with the initial guidance we gave at the beginning of the year.

**Rachel Rodriguez**
*Investor Relations Contact, McKesson Corp.*
A

Next question, please.

**Operator**: And next will be Lisa Gill with JPMorgan.

**Lisa C. Gill**
*Analyst, JPMorgan Securities LLC*
Q

Great. Good afternoon, everyone. I hope everyone is safe in Texas. Just wanted to go back to a couple of comments that you made around US drug distribution. One would be the renewal with CVS through 2027. Just want to understand if there's anything new or nuance to that relationship?

And then secondly, as we think about oncology within US drug distribution, Britt, I don't know if it was you or Brian that made the comment that you're going to see higher growth and higher margin there. At what point does that become big enough that that actually drives the margin? Or is that part of what we're seeing in the margin improvement today? Just any kind of guardrails you could give us around how to think about that on a go-forward basis as that business continues to grow.

**Brian S. Tyler**
*Chief Executive Officer & Director, McKesson Corp.*

A

Sure. Look, we were obviously – I think last quarter, we shared we had a binding LOI with CVS. We've just finalized that contract work, Lisa. We've been partnering with CVS for a long time. We're incredibly proud to support the work they do and be affiliated with them. I would not say that the services that we're providing has materially changed. And so we're thrilled to have the opportunity to extend that to 2027.

In terms of oncology, I mean, we call it an ecosystem because we think it all sort of reinforces each other. So as we do things like bring practices into the network, that gives us more access to data, which supports oncology. It gives us more purchasing power and it supports our GPO business. And so we've been really pleased with the progression in the oncology business and our ability to scale out in each of those dimensions, but each piece does help to reinforce the other piece. And we continue to think oncology is a very large market opportunity, in excess of $50 billion, and that we have the assets that position us quite well to succeed in the long term here.

**Britt Vitalone**
*Chief Financial Officer & Executive Vice President, McKesson Corp.*

A

And Lisa, maybe what I would add, what we've done over the last year or two through the development of Ontada, through the partnerships with Sarah Cannon Research Institute and Genospace, we're moving up the value chain. And so we're leveraging the scale that we have in The US Oncology Network, the distribution scale, the GPO scale that Brian just talked about. We're adding more practices as Brian referenced earlier. And by moving up the value chain with more scale, we're very optimistic that that's going to add to margin over the coming years.

**Rachel Rodriguez**
*Investor Relations Contact, McKesson Corp.*

A

Next question, please.

**Operator**: And next will be Eric Percher with Nephron Research.

**Eric Percher**
*Analyst, Nephron Research LLC*

Q

Thank you. I appreciate the commentary on fiscal year 2023 relative to long-term guidance targets. I believe last year at this time, you provided a little bit of forward commentary in advance, the formal guidance on the factors that might be worth keeping in mind as we all model fiscal year 2024. What would you call out relative to those items that have been helping 2023 and may or may not drive you above/below long-term guidance next year?

**Britt Vitalone**
*Chief Financial Officer & Executive Vice President, McKesson Corp.*

A

Thanks for the question, Eric. I tried to address a little of that in my comments, but maybe I can capture it here. I think there's really a handful of items that we think could be impactful as we go forward. Clearly, we talked about the stabilization of prescription transactions and patient mobility and utilization seems to be quite stable. We saw prescription volume growth of about – roughly about 5% in our third quarter, so that seems to be in line with what we've seen in the last few quarters.

Certainly, biosimilar acceleration, we're going to see more biosimilars coming to market. We've got just over two dozen that are on the market today and more are coming. Some recent announcements certainly back that up. I'd say the timing and size of the growth investments that we make and really the timing of our integration, some of the acquisitions that we made, we think could be very impactful in a positive way.

And then I think there are a handful of other items. The trajectory of COVID, we think that that's going to go into the commercial pipeline here in 2023. Our contract goes through July of 2023. It doesn't mean that those services and products are going to go away. So the pace and trajectory of that will certainly be impactful.

And we have a very strong balance sheet. We expect to continue to deploy that balance sheet in a very capital-accretive way, whether that's returning to shareholders or, as you've seen us do here recently, more towards acquisitions that are right on strategy. And clearly, we have the opportunity to invest organically as well.

So there's a lot of really positive things that are going on. There are some things that could go the other way in terms of trajectory of COVID as an example. But we feel like we're really well positioned against all of those items.

**Brian S. Tyler**
*Chief Executive Officer & Director, McKesson Corp.*

A

Yeah. I mean, the macro backdrop remains a bit dynamic, right? We've got China open, China closed. Inflation, obviously, workforce dynamics we've dealt with. We successfully, I think, contemplated that in our FY 2023 guidance. Did not really assume any material impact and I think it's played out that way, and we'll be thoughtful about those as we go into 2024 as well.

**Rachel Rodriguez**
*Investor Relations Contact, McKesson Corp.*

A

Next question, please.

**Operator**: And next will be Charles Rhyee with Cowen. Charles, your line is open.

**Brian S. Tyler**
*Chief Executive Officer & Director, McKesson Corp.*

A

Charles, are you there?

**Charles Rhyee**
*Analyst, Cowen & Co. LLC*

Q

Hi. Can you hear me now?

**Brian S. Tyler**
*Chief Executive Officer & Director, McKesson Corp.*

A

Charles, yes, we can hear you.

**Charles Rhyee**
*Analyst, Cowen & Co. LLC*

Q

Okay. Great. Thanks. Thanks for taking the question. Hey. I just wanted to touch a little bit on the Medical segment. Obviously, if we back out COVID, very strong growth here. And just wanted to dig a little deep to understand what's driving it. I know you mentioned the primary care business. But maybe if you can go a little deeper into that. Is that a – is there any changes in product mix? Or is this really – or – because I don't think it's probably volume growth per se, but anything about your customers and their growth or new customer wins. Anything that you can kind of call out there would be helpful. And because the 25% obviously, is higher than the full year. And how should we think about that, maybe to Eric's question earlier, about thinking about 2024 as well.

**Brian S. Tyler**
*Chief Executive Officer & Director, McKesson Corp.*

A

Go ahead, Britt. You want to take it?

**Britt Vitalone**
*Chief Financial Officer & Executive Vice President, McKesson Corp.*

A

Yeah. I would say that in the quarter, we identified that we had some strength in some of our sourcing programs, and that's really what drove above the trend that we've been seeing for the last really several years now. At our Investor Day, we talked about a long-term target rate of around 10%. We certainly are growing a little bit faster than that this year. Certainly, the volumes have been strong. And obviously, the sourcing programs were really a good contributor in the quarter.

I think as you think about going forward, clearly, we've given you the guidance for 2023. But I would anchor you around the long-term growth rates that we've seen now really for the last three to four years. Those are good growth rates. There are good margins within this business. And we think that the primary care business is really going to be supportive of that 10% growth rate going forward.

**Rachel Rodriguez**
*Investor Relations Contact, McKesson Corp.*

A

Next question, please.

**Operator**: And the next question will be from the line of George Hill with Deutsche Bank.

**George Hill**
*Analyst, Deutsche Bank Securities, Inc.*

Q

Good evening, guys, and thanks for taking the question. Britt, I'm going to ask you to double check my math on this, which is if I look at your guidance for the Pharma segment for the full year, you're basically – you have it growing 200 basis points faster for the balance of the year ex-COVID, which I assume if I annualize, is going to look like something greater than 6% versus preliminary expectations or at least going into the quarter. I guess, could you talk about what's driving that at the core? And can we think about kind of the sustainability of the pockets of strength you're seeing in that business? Thank you.

**Britt Vitalone**

*Chief Financial Officer & Executive Vice President, McKesson Corp.*

A

Yeah. Thanks, George. So we did raise the guidance for the full year to 7% to 9%, excluding COVID-related items, and we're very pleased with the performance of the segment. As I talked about in my comments, there's really a number of factors here. We've got stable prescription utilization. As I mentioned, we saw – we're seeing about 5% based on IQVIA data in the third quarter. We're certainly seeing strength in our oncology platform. I think we just talked about some of the factors that are driving that. We're adding practices and we're certainly moving up the value chain from that perspective.

And we're seeing growth, really stable growth in specialty providers as well as in health systems. And so all of those things are performing quite well. And that's also why I talked about that we're expecting now that we're going to grow faster than long-term target growth rate that we gave you at Investor Day and that we've reaffirmed in previous quarters. So we think all of those things are really positive contributors. And that's why we're seeing faster growth than we would expect, faster than the 4% long-term target growth rate that we gave you previously.

**Rachel Rodriguez**

*Investor Relations Contact, McKesson Corp.*

A

Next question, please.

**Operator**: And next will be Steven Valiquette with Barclays.

**Steven Valiquette**

*Analyst, Barclays Capital, Inc.*

Q

Great. Thanks. Good afternoon, everyone. Thanks for taking the question. Yeah. I guess, separate from all of the helpful color around the COVID profit streams, are you really able to comment just on how much flu may have been a key factor in the earnings upside in the quarter, either in the Pharma segment or the Medical segment? Thanks.

**Britt Vitalone**

*Chief Financial Officer & Executive Vice President, McKesson Corp.*

A

Yeah. As we've talked about previously, this has been a stronger flu season than we've seen historically. It really started in our first quarter. We talked about in our first quarter that there was an extension of the illness season from our fiscal 2022.

It's not a material driver to the enterprise. It certainly does drive more visits. We're seeing that the illness season is driving not only vaccines and test flu test kits but also some combo kits, which is – which started last year. So it's not a material driver to the enterprise. It certainly does drive more foot traffic and that certainly is beneficial to other products and services that we have, not only in Medical but in Pharma.

**Rachel Rodriguez**

*Investor Relations Contact, McKesson Corp.*

A

Next question, please.

**Operator**: And next question will be from Brian Tanquilut with Jefferies.

**Brian Tanquilut**
*Analyst, Jefferies LLC*
Q

Hey. Good afternoon, guys. I guess just to follow up on Lisa's question and Britt's comments on the oncology side. It sounds like you guys are looking to get more aggressive with the roll-up of Oncology Networks, and it seems like there's consolidation there. So as I think of catalysts and maybe like big moves in that space, I mean, do you see opportunity with – or should we be thinking about the Sarah Cannon partnership as an opportunity that could bring a big chunk of new doctors into the network in the coming years? Or how should we be thinking about that? Thanks.

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**Brian S. Tyler**
*Chief Executive Officer & Director, McKesson Corp.*
A

Well, oncology is clearly one of the key growth priorities we've identified for the company and talked a lot about over the last years. And there are various capabilities within our oncology ecosystem, distribution as an anchor, GPO as an anchor, our practice management business you saw on, clearly important, the innovation we've done around Ontada and the most recent addition of Genospace and the Sarah Cannon joint venture.

So we think all of these things sort of add to our differentiation, add to the attractiveness of McKesson as a service provider and a partner in this area. We've been really happy to be continuing to add to the growth of The US Oncology Network. We do it in a very disciplined way. We have a model that works for us and any acquired practices need to be able to operate consistent within that model. But as clearly our actions this last quarter indicate, we have opportunities to continue to grow and expand. And we think that that's part of our model and we expect that we can continue that into the future.

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**Rachel Rodriguez**
*Investor Relations Contact, McKesson Corp.*
A

And we have time for one more question, please.

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**Operator**: Certainly. That question will come from the line of A.J. Rice with Credit Suisse.

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**A. J. Rice**
*Analyst, Credit Suisse Securities (USA) LLC*
Q

Thanks. Hi, everyone. Maybe just to get you to expand, if possible, a little bit more on your comments around specialty and the development of biosimilars. I guess if you look out over the next few years, we have a significant number converting. I know it depends in your business on how that drug is administered today and how it's – the patient receives it, but as to how much benefit you'll derive. But is there a way to talk about how you see that progressing over time?

And then maybe another aspect of that is we hear from a number of players that they're expecting to put more resources behind specialty and grow. Can you give us a little bit of a sense of how you assess the competitive landscape at this point and your positioning?

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**Brian S. Tyler**
*Chief Executive Officer & Director, McKesson Corp.*
A

Well, the – I would start by saying that the contributions from biosimilars has been increasing over the past years. We do think the pipeline holds a lot of promise. It continues to strengthen, and we think this could be a long-term opportunity really exists in front of us. I mean to date, there's 40 approved biosimilars, 25 launched, I guess, maybe 26 because if you count today's news on HUMIRA. And the impact of those are going to really be dependent on the rates of adoption, things like the interchangeability.

For us, clearly, the channel will matter. Part B is we have more services to offer and more support we can provide to those biosimilars in Part B. Part D will be less impactful. But I think we continue to look at the majority of the opportunity being ahead of us. I do think this market is still young, and I think as people get more experience with biosimilars, we would be hopeful that adoption rates would continue to accelerate.

But it depends on things like pricing strategies that the innovator adopts and the biosimilar comes to market with. So there's a lot of dynamics that I think are still playing out like they always do in a young market. But we're in the very early days, and we believe biosimilars will be good for our business model going forward.

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## Brian S. Tyler

*Chief Executive Officer & Director, McKesson Corp.*

Okay. Well, thank you, everyone, for joining our call this evening. Appreciate, as always, the thoughtful questions. I want to thank Carrie, our operator, for facilitating this call. Let me just wrap up by saying McKesson delivered really good third quarter results. And it's really driven by the continued momentum in our underlying business.

I'm confident in our ability to consistently execute on our company priorities and drive sustainable long-term growth as a diversified healthcare services company. None of this is possible without Team McKesson. So I'd like to thank everyone for their dedication, for the big and small actions they take every day to help our customers, our partners and our patients. I'm proud to be a member of and the leader of Team McKesson. Thanks again, everyone, for joining our call. I hope you all have a great evening.

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**Operator**: Thank you for joining today's conference call. You may now disconnect, and have a great day.