PARTICIPANTS

Corporate Participants

Brian Patrick McKeon – Executive Vice President, Chief Financial Officer & Treasurer, IDEXX Laboratories, Inc.
Jonathan J. Mazelsky – President, Chief Executive Officer & Director, IDEXX Laboratories, Inc.

Other Participants

Nathan Rich – Analyst, Goldman Sachs & Co. LLC
Ekaterina V. Knyazkova – Analyst, JPMorgan Securities LLC
Michael Ryskin – Analyst, BofA Securities, Inc.
Ryan Daniels – Analyst, William Blair & Co. LLC
Jonathan D. Block – Analyst, Stifel, Nicolaus & Co., Inc.
David Westenberg – Analyst, Piper Sandler & Co.
Mikaela Franceschina – Analyst, Barclays Capital, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Good morning, and welcome to the IDEXX Laboratories Second Quarter 2023 Earnings Conference Call. As a reminder, today's conference is being recorded. Participating in the call this morning are Jay Mazelsky, President and Chief Executive Officer; Brian McKeon, Chief Financial Officer; and John Ravis, Vice President, Investor Relations.

IDEXX would like to preface the discussion today with a caution regarding forward-looking statements. Listeners are reminded that our discussion during the call will include forward-looking statements that are subject to risks and uncertainties that could cause actual results to differ materially from those discussed today. Additional information regarding these risks and uncertainties is available under the forward-looking statements notice in our press release issued this morning as well as in our periodic filings with the Securities and Exchange Commission, which can be obtained from the SEC or by visiting the Investor Relations section of our website, idexx.com.

During this call, we will be discussing certain financial measures not prepared in accordance with generally accepted accounting principles, or GAAP. A reconciliation of these non-GAAP financial measures to the most directly comparable measures are provided in our earnings release, which may also be found by visiting the Investor Relations section of our website.

In reviewing our second quarter 2023 results, please note all references to growth, organic growth and comparable growth refer to growth compared to the equivalent period in 2022 unless otherwise noted.

To allow broad participation in the Q&A, we ask that each participant limit their questions to one with one follow-up if necessary. We appreciate you may have additional questions, so please feel free to get back into the queue, and if time permits, we'll take your additional questions.

Today's prepared remarks will be posted to the Investor Relations section of idexx.com after the earnings conference call concludes. I would now like to turn the call over to Brian McKeon.

Brian Patrick McKeon, Executive Vice President, Chief Financial Officer & Treasurer, IDEXX Laboratories, Inc.

Good morning, and welcome to our second quarter earnings call. Today, I'll take you through our Q2 results and review our updated financial outlook for 2023.

In terms of highlights, IDEXX achieved strong growth and financial performance in the second quarter, aligned with our full year performance goals. Overall revenues increased 10% organically, supported by 12% organic growth in CAG Diagnostic recurring revenues, with double-digit gains in US and international regions.

Key execution metrics remain very strong globally, reflected in record second quarter premium instrument placements, continued solid new business gains and sustained high growth in recurring veterinary software revenues.

Operating profit results were ahead of our expectations, reflecting solid gross margin gains and operating expense leverage, both benefiting from strong CAG recurring revenue growth.

For the first half of 2023, we achieved 10% overall organic revenue growth and nearly 12% growth in CAG Diagnostics recurring revenues. We also achieved better than targeted operating margin improvement. We've made positive refinements to our full year operational outlook incorporating this performance, which we'll discuss later in my comments.

Let's begin with a review of our second quarter results. Second quarter organic revenue growth of 10% was driven by 11% CAG gains and 9% organic growth in our Water business. Overall organic revenue growth was constrained by modest gains in our LPD business and approximately $3 million of headwind related to lower OPTI Medical revenues, reflecting the wind down of our human COVID testing business.

CAG Diagnostics recurring revenue increased 12% organically, reflecting 12% gains in the US and 10% growth in international regions. CAG Diagnostics recurring revenue growth in Q2 was supported by global net price gains at the higher end of our targeted 8% to 9% improvement range for the first half of 2023.

Overall organic revenue growth was supported by 13% growth in veterinary software and diagnostic imaging revenues. CAG instrument revenues were down 6% organically, reflecting comparisons to high prior year levels, program pricing effects and global mix. IDEXX CAG Diagnostics recurring revenue growth remained solidly above sector growth levels.

In the US, we achieved a consistent, strong 1370 basis point growth premium in Q2 compared to same-store US clinical visit growth levels, which declined an estimated 1.3% in the quarter. These results reflect benefits from IDEXX execution drivers, including higher net price realization. Solid US volume growth was supported by new business gains, high customer retention levels and continued increases in diagnostics frequency and utilization at the practice level.

International CAG Diagnostics recurring revenue growth improved organically to 10% in Q2, reflecting positive volume gains and benefits from higher net price realization. International results were also supported by strong IDEXX execution, reflected in sustained new business gains and record Q2 premium instrument placements, which supported a double-digit expansion of our premium instrument installed base. Double-digit growth rate benefits from IDEXX execution offset impacts from challenging international macro conditions, which continued to pressure same-store volume growth trends in the quarter.

Globally, Q2 results were supported by strong growth of IDEXX in clinic CAG Diagnostic revenues. IDEXX VetLab consumable revenues increased 15% organically with double-digit gains in US and international regions. Consumable gains were supported by 11% year-on-year growth in our global premium instrument installed base, reflecting strong gains across our Catalyst, Premium Hematology and SediVue platforms.

We placed 4,740 CAG premium instruments in Q2, an increase of 7% year-on-year compared to very strong prior year levels, which included benefits from our international launch of ProCyte One.

Catalyst placements increased 15% globally, reflecting 8% gains in the US and 19% placement growth in international regions. The quality of instrument placements continues to be excellent demonstrated by 9% global growth in new and competitive Catalyst placements and solid gains in EVI metrics.

ProCyte One momentum also continues to be strong globally, reflected in a global installed base of approximately 10,800 instruments.

Global Rapid Assay revenues expanded 12% organically in Q2, driven by strong growth in the US, reflecting solid volume gains and benefits from higher net price realization. Global lab revenues increased 9% organically, reflecting double-digit gains in the US and mid-single-digit growth in international, with growth in international regions moderated by macro-economic impacts which pressured same store sales.

In other areas of our CAG business, veterinary software and diagnostic imaging revenues increased 13% organically. Results were supported by continued high levels of organic growth in recurring software and digital imaging revenues and ongoing momentum in cloud-based software placements.

Water revenues increased 9% organically in Q2, reflecting continued solid gains in the US, Europe and Latin America, including benefits from net price improvement. The integration and performance of our recent TECTA-PDS acquisition continues to progress well, expanding our capabilities in Water safety testing and adding approximately 2% to reported Water growth.

Livestock, Poultry and Dairy revenue increased 1% organically, as strong gains in the US were offset by impacts from lower herd health screening revenues related to reduced China import testing.

Turning to the P&L, Q2 profit results were supported by solid gross profit gains. Gross profit increased 11% in the quarter as reported and 13% on a comparable basis. Gross margins were 60.7%, up 160 basis points on a comparable basis. These gains reflect benefits from higher net price realization, lab productivity and operational initiatives, improvement in software service gross margins and business mix, which offset inflationary cost effects.

As expected, reported gross margin gains were moderated by a 60 basis point negative impact related to foreign exchange changes, including the lapping of prior year hedge gains. While foreign exchange trends have improved, we're expecting approximately 70 to 80 basis points of negative impact in year-on-year reported gross margin comparisons in the second half of 2023, as we work through lapping of $18 million of prior year foreign exchange hedge gains.

On a reported basis, operating expenses decreased 17% year-on-year, reflecting a 26% favorable growth rate impact from comparisons to prior year levels, which included $80 million in discrete R&D investment. Adjusting for this effect, operating expense growth was modestly below revenue growth in the quarter, supporting operating margin gains.

EPS was $2.67 per share in Q2, an increase of 71% as reported. On a comparable basis, EPS increased 77%, including approximately 54% of growth rate benefit from lapping the $0.72 per share prior year impact from discrete R&D investments.

Foreign exchange reduced operating profits by $8 million and EPS by $0.07 per share in the quarter, including impacts from the lapping of $6 million in prior year hedge gains. Impacts from 2023 foreign exchange hedges were limited in the quarter.

Free cash flow was $173 million in the second quarter. On a trailing 12-month basis, our net income to free cash flow conversion ratio was 75%. For the full year, we're maintaining our outlook for free cash flow conversion of 80% to 90%, including estimated capital spending of approximately $180 million.

Our balance sheet remains in a strong position. We ended the quarter with leverage ratios of 0.9 times gross and 0.7 times net of cash. Share repurchases over the last year supported a 1% reduction in diluted shares outstanding. We didn't allocate capital to share repurchases in the second quarter, as we manage our balance sheet relatively more conservatively in the current interest rate environment.

Turning to our 2023 P&L outlook. We're refining our full year outlook to incorporate our solid first half operating results and updated estimates for foreign exchange impacts. Our updated full year guidance for reported revenues is $3,660 million to $3,715 million, reflecting an 8.5% to 10% organic growth range. This outlook includes a $15 million favorable adjustment for foreign exchange changes, which we now estimate will have a relatively flat full year impact on reported revenue growth at the rate shown in our press release.

In terms of our operational growth outlook, we're maintaining our performance goals aligned with the high-end of our guidance range of 10% overall organic revenue growth, supported by 11% CAG Diagnostic recurring revenue gains. This reflects expectations for consistent strong levels of IDEXX execution, aligned with H1 trends.

Our outlook incorporates approximately 1% of expected H2 headwinds for CAG Diagnostics recurring revenues from equivalent days effects. Consistent with earlier guidance, our high-end outlook for CAG Diagnostics recurring revenue growth reflects expectations for 6% to 7% net price gains and a relative flattening of US same-store clinical visit growth trends in H2.

We've raised the low end of our full year organic revenue growth outlook by 1% to reflect our strong first half performance. We've also made positive adjustments to our outlook for operating margin performance in 2023. Our updated outlook is for reported operating margins in the range of 29.3% to 29.7% for the full year. At the high-end, this reflects an outlook for approximately 360 basis points in comparable operating margin expansion. This includes approximately 280 basis points and combined benefit from the $16 million Q1 customer contract resolution payment and the lapping of $80 million of discrete R&D investment in the second quarter of 2022.

Our operating margin outlook reflects expectations for moderated year-on-year comparable gross margin gains in the second half compared to strong prior year levels.

We continue to project that foreign exchange will reduce operating margins by approximately 60 basis points this year, primarily related to impacts from the lapping of $26 million in 2022 hedge gains. We estimate that foreign exchange impacts will decrease EPS by approximately $0.21 per share for the full year, with approximately $0.02 per share of negative impact in the second half, including effects from hedge gain lapping.

Our updated EPS outlook is $9.64 to $9.90 per share. This is an increase of $0.23 per share at midpoint reflecting $0.17 in benefit from our raised operational outlook and $0.06 in combined benefit from refined interest expense and foreign exchange estimates.

In terms of our operational outlook for Q3, we're planning for organic revenue growth at the lower end of our updated full year growth range incorporating expected impacts from approximately 1% of equivalent day headwinds. We expect foreign exchange to provide approximately 1.5% in reported growth rate benefit in the quarter.

We're planning for operating margins in the 28.5% to 29% range, reflecting expectations for relatively consistent comparable operating margin performance, adjusting for unfavorable foreign exchange margin impacts of approximately 50 basis points driven by hedge gain lapping.

We've provided details on our updated full year outlook in the press release tables and earnings snapshot. That concludes our financial review.

I'll now turn the call over to Jay for his comments.

Jonathan J. Mazelsky, President, Chief Executive Officer & Director, IDEXX Laboratories, Inc.

Thank you, Brian, and good morning.

IDEXX once again delivered strong results supported by outstanding execution in the second quarter. We advanced our strategy by engaging customers with integrated testing solutions that support their mission and address real world clinical and practice problems. Demand for medical services remains high and veterinarians see diagnostics as a core enabler to guide individualized best care. As a result, we saw strong diagnostic sector revenue growth, with continued gains in diagnostic testing frequency and utilization.

IDEXX remains well positioned to further benefit from these trends thanks to our decades-long focus on diagnostics and the software solutions that deliver key, differentiated insights into the patient's health.

IDEXX's strong results are reflected in double-digit total company organic revenue growth, supported by expansion of CAG Diagnostics recurring revenues across regions. For the first time ever, US revenues exceeded $1 billion in the first half of 2023. IDEXX execution drivers continue to fire on all cylinders as reflected in our financial results, including growth in high quality premium instrument placements, sustained high customer retention levels, contribution from new business gains, and net price realization that remains aligned with our expectations.

IDEXX commercial teams delivered yet another record quarter of global premium instrument placements, building off high prior year levels and supporting solid EVI gains for the quarter.

IDEXX diagnostics and software solutions deliver key insights and productivity improvements through workflow transformation. These results demonstrate that a greater number of clinicians are partnering with IDEXX with the aim to deliver higher care standards and crucial efficiency gains. This support continues to be an important given persistent clinic productivity constraints and a dynamic macro backdrop.

Today I'll discuss how IDEXX delivered continued strong performance through key strategic initiatives aimed at driving sector development. I'll start by providing an update on our global commercial execution. It's a key component in driving increased testing utilization at both existing customers as well as new-to-IDEXX accounts.

Veterinarians around the world seek testing solutions that provide them with key diagnostics insights necessary to choosing and delivering the right care path in an efficient and intuitive way. IDEXX commercial teams, as trusted advisors, seek to provide the most appropriate solution given a practice's objectives. There is a deep appetite for point of care solutions that deliver the right performance, ease-of-use, workflow integration and economics.

Therefore, it was gratifying to see a record second quarter of global premium instrument placements with record placements in both the US and internationally. Second quarter premium placements reflected growth across regions and platforms highlighting the value that clinicians across different geographies at various stages of practice maturity see in our highly innovative platforms and integrated ecosystem.

An important dimension of this success is our menu of customer-friendly marketing programs to adopt IDEXX innovations. The result was continued solid gains in EVI and excellent contribution from new business gains, including a new, key US corporate account.

Very strong ongoing placement performance, and our solid relationships with accounts of all types, reinforces our confidence in future flow-through of recurring revenues and our ability to address the estimated 220,000 global instrument placement opportunity.

Our commercial performance this year demonstrates that we have developed the right suite of innovative products to address this significant opportunity. ProCyte One is a great example of this. It's our newest, easy-to-use premium hematology platform. ProCyte One boasts efficiency gains including load-and-go reagents and a pay-per-run model, while still delivering uncompromised accuracy. It has been a key driver of strong premium hematology placements since its launch in early 2021, and supported record second-quarter premium hematology placements.

Not only does the growing hematology installed base support flow-through of recurring revenues, but also drives our broader in-clinic business. Sustained mid-90% attach rates with Catalyst provide a multiplier benefit that drives growth in our customer base and helps customers realize the benefits of an integrated IDEXX diagnostics suite within their clinics.

These multiplied effects supported the strong 15% global growth achieved in Catalyst placements in Q2 with strong gains globally in new and competitive accounts. ProCyte One also helps to advance our long-term growth strategy in international regions, where most veterinarians are trained to do hematology testing when assessing a patient's baseline health.

Strong second quarter performance included double-digit CAG Diagnostics recurring revenue growth also benefited from the country-level commercial expansions we began in mid-2020. By increasing the density of our commercial reach, IDEXX sales professionals are better able to build relationships with veterinarians and communicate the benefits of diagnostics and software solution utilization and how IDEXX can support them on that journey.

The global opportunity we have identified is significant, and these expanded commercial teams are the tip of the spear in our multi-modality strategy to drive continued sector development. Benefits from these investments are highly encouraging as evidenced by strong installed base growth supported by excellent placements at new and competitive accounts, revenue gains from new business, and improving customer engagement levels in key international regions.

Of additional note, we have also executed a modest expansion of US territories and customer facing professionals based on highly attractive opportunities still before us in our largest geography. We anticipate all hiring to be completed and in place by the end of this year.

In addition to high quality and quantity of instrument placements across regions in Q2, commercial execution helped drive continued adoption of IDEXX innovations, included – including within our rapid vector-borne disease screening franchise. Our VDC teams have done a great job communicating the health benefits of a full vector-borne disease screen versus Heartworm-only testing. We see, consequently, 4Dx Plus making up a greater share of in-clinic vector-borne disease revenue. This adoption is supported by our growing installed base of SNAP Pros, which provides an integrated solution while managing workflow and ensuring charge capture.

These focused commercial efforts, combined with relevant and easy-to-use products, highlights how we continue to build our customer base which positions IDEXX well for long-term growth.

Building on these commercial efforts, IDEXX's growth will continue to benefit from advancement of our innovation strategy, a core component of which is expanding our highly accurate and relevant test menu. We made a significant step forward in this area during the second quarter when we announced the launch of the IDEXX Cystatin B Test in our North American Reference Lab network.

This novel marker leverages IDEXX IP to help clinicians detect kidney injury, a hard-to-diagnose condition that comprises approximately one-third of all kidney cases seen by veterinarians. Renal care is a critical area for diagnostics insights since the kidneys regulate blood pressure, electrolyte balance, and red blood cell production while also removing toxins.

By adding Cystatin B to our renal portfolio, and by pairing it with IDEXX SDMA, our customers will have access to the most comprehensive view of kidney health, helping them uncover structural injury and impaired kidney function. What's even more exciting is we will leverage our SDMA playbook to support adoption by including Cystatin B in test panels for approximately 2 million patients annually at no additional cost helping clinicians realize the benefits of IDEXX's world class diagnostics and deliver a higher standard of care to their patients.

IDEXX diagnostics solutions, like the innovative Cystatin B test, when used in an integrated way with our software portfolio, can contextualize an individual patient's health status and support the veterinarian with interpretation and drawing out the appropriate clinical insights. Our software portfolio which includes a full stack of solutions, many of which leverage cloud technology touches all areas of the veterinary clinic.

From enabling patient check-ins and the full diagnostics workflow to pet owner communication and charge capture, IDEXX software solutions create a connected ecosystem that supports greater diagnostics utilization while also helping our busy customers be more efficient.

A key driver of customer interest we see in our software solutions is driven by the high demand customers are seeing for medical services. These solutions appeal to both independent and especially corporate customers, who are increasingly focused on using software to standardize their workflow at scale.

Given this backdrop of high demand for pet healthcare services, busy clinics continue to appreciate the value of cloud-based products, as these intuitive and easy to administer products allow them to spend more time focusing on their patients that walk-in the door rather than on time-consuming back-office tasks.

And IDEXX cloud-native products, including our ezyVet and Neo PIMS and Web PACs imaging software continue to be in high demand as a response to this trend. For example, second quarter cloud-based PIMS once again comprised over 90% of total PIMS placements, and as a result, make up nearly 50% of our PIMS installed base. This is a trend we expect to continue and are well positioned to address.

In our digital imaging business, record first-half instrument placements supported double-digit organic growth and demonstrate that customers are increasingly choosing IDEXX to partner on this piece of their business. It helps grow our base for future high-margin recurring revenues.

One driver of this interest is continued innovation of our Web PACs software, which makes it even easier for clinicians to interpret and identify hard-to-detect internal abnormalities. The result of these efforts is an excellent customer experience, which helped earn a world class NPS rating for our diagnostic imaging business, one proof point of the solid overall experience that customers of all types have with IDEXX.

This concludes our review of our second quarter results. I would like to extend my thanks to the nearly 11,000 IDEXX employees who helped deliver continued strong performance aligned with our purpose of enhancing the health and well-being of pets, people and livestock. We look forward to building on this progress.

Before we move to Q&A, I would like to remind you that we'll be hosting our annual Investor Day in August, beginning with a management dinner on Wednesday, August 9, followed by presentations at our global headquarters in Westbrook, Maine on Thursday, August 10 at 8 AM. Thursday's event will also be livestreamed and recorded via idexx.com for those who cannot make it in person. This is an exciting opportunity for the IDEXX leadership team to provide updates on our strategy, execution drivers, innovation cycle and long-term growth potential.

Participating will be members of my senior management team including Dr. Tina Hunt, Executive Vice President, Strategy, Sector Development and Global Operations; Dr. Mike Erickson, Senior Vice President and General Manager, Point of Care Diagnostics; Mike Lane, Executive Vice President and General Manager for Reference Laboratories & Information Technology; Michael Schreck, Senior Vice President and General Manager, Veterinary Software and Services and Corporate Accounts; and Brian McKeon, Executive Vice President and Chief Financial Officer.

We're also excited to host a live customer conversation led by Jim Polewaczyk, Executive Vice President and Chief Commercial Officer, to provide a firsthand view of the role of diagnostics within the clinic and how IDEXX is supporting our customers in adapting to the dynamic sector backdrop. The event will last approximately four hours and will conclude with a Q&A session.

And with that, we'll end the prepared section of the call and open the line for Q&A.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] We'll take our first question from Nathan Rich with Goldman Sachs. Please go ahead.

<Q – Nate Rich – Goldman Sachs & Co. LLC>: Great. Good morning. Thanks for the questions. Two questions on volumes. I guess first in the US. Could you maybe talk, Brian, about how clinical visits trended over the course of the quarter? I know you kind of said that it softened earlier in the quarter. Just curious how the quarter played out relative to your expectations and kind of what you're looking for to see that flattening over the balance of the year.

And then on international, what drove the improvement in the international CAG growth this quarter? And I think kind of despite the improvement, Reference Lab kind of remains soft. Why do you think you maybe haven't seen more improvement in Reference Lab volumes? And can you maybe talk about expectations there for the back half of the year? Thank you.

<A – Brian McKeon – IDEXX Laboratories, Inc.>: Thanks for your questions, Nate. On the first question, we saw post-January relatively similar clinical visit trends in the data. I think with hindsight, January benefited from the year-on-year COVID lapping. And overall for the first quarter, it was flat, but they benefited from that dynamic. And I think the clinical visit trends through Q2 were largely consistent. This was consistent with our expectation. We thought we'd see a reduction in the headwinds from the clinical visit capacity pullback that happened last year, and that we were still working through some compares on that front in the first half. And so that informed how we were thinking about the second half that we'd see that normalize and hopefully, over time, improve given the strong underlying demand that we believe is out there. So that's sort of the US story.

Let me give some context on international. I'm sure Jay can add to this. The strength in international came from our in-clinic business, just a very strong growth in our instrument placements, customer engagement, supported strong consumable gains. And so, I think that's directly related to our executional focus. And as you pointed out, Labs were relatively consistent. We're still seeing the – have seen the macro headwinds relatively more in international markets. That's been a consistent story. And so that moderated what were double-digit growth rate benefits from the executional drivers – that enabled us to get to double-digit overall growth in international markets.

<A – Jay Mazelsky – IDEXX Laboratories, Inc.>: Yeah. And just to add to that, Nate, from a higher-level standpoint, the clinic economics and overall health of the clinics really is healthy. I think revenue, we showed that revenue is growing nicely. So it's certainly not a demand dynamic. And as Brian said, internationally, we've been benefiting really over a number of quarters of record placements. ProCyte One obviously fits well and leverages and multiplies the impact we've been able to have on total in-clinic placement. So I think very strong execution. We're now seeing the benefits of the consumables growth, and that has a small ramp to it. But I think the business is healthy, and we saw positive volume growth in Q2 internationally. So I think the clinics are working through the type of capacity constraints and labor challenges that they've had earlier. And we expect that to continue over time.

<Q – Nate Rich – Goldman Sachs & Co. LLC>: Great. Thanks for the details.

Operator: We'll move to our next question from Chris Schott with JPMorgan. Your line is now open. Please go ahead.

<Q – Ekaterina Knyazkova – JPMorgan Securities LLC>: Hi. This is Ekaterina from JPMorgan on for Chris. Thank you so much for taking our questions. So first, just on pricing. I know you probably can't give too much specifics. But directionally, any initial thoughts on how you're going to approach price increases in 2024? On one hand, obviously, inflation has slowed, but then you also probably could see some upward pressure on cost. So, does that warrant larger prices? Just how are you thinking about 2024 price increases?

And then the second question is, so as you think about both clinical visit growth and then utilization, any major differences between what you're seeing for your corporate clinic accounts versus your non-corporate, but owned – privately owned accounts? Thank you, so much.

<A – Jay Mazelsky – IDEXX Laboratories, Inc.>: Good morning.

<A – Brian McKeon – IDEXX Laboratories, Inc.>: Thanks for your question. On the pricing front, first, I just want to reinforce. We have a consistent outlook for the second half of 2023 for 6% to 7% overall net price improvement related to CAG Diagnostic recurring revenues. We're not prepared to share our plans for 2024. What I would note is that we'll have, as we've had in the past, a very thoughtful approach that's aligned with long-term sector development and the value that we deliver through our solutions and our innovations. And we'll evaluate and incorporate inflationary dynamics as part of that approach as we get closer to next year.

<A – Jay Mazelsky – IDEXX Laboratories, Inc.>: Yes. Just a couple of words about pricing. To Brian's point, we – from a philosophical standpoint, we want to make sure we continue to deliver really strong value. And we think that our pricing reflects the fact that we continue to do that. We see really very high retention levels in our business. We see an increase in adoption and utilization. So from the standpoint of, I think, customer receptivity, the – we think our pricing is appropriate given the circumstances.

If you think about our latest menu release in Reference Labs, that's Cystatin B, it's a great example of how we add value, that we're increasing the menu, 2 million patients on a global basis – annual global basis are going to benefit this – benefit from this. We're not increasing the price of those panels. I think it's just a great example of how we try to keep that value equation appropriately aligned to what our customers need.

In terms of corporate versus independent practices, a couple of dynamics to keep in mind. Largely, we don't see big differences. Obviously, there's differences in things like the size of the practice. Corporate practices tend to be a bit larger. There are more specialty practices owned by corporates. They're focused, I think, increasingly on growth. We've seen nice interest, not just in our solutions like in-clinic premium analyzers, but also software solutions as they really try to operate the businesses in a more standardized way. They're interested in the same type of diagnostic solutions that independent practices are. We see a lot of interest in things like preventive care, for example, because it's a great way of, I think, continuing to engage pet owners. And clients really uncover, I think, disease that may be otherwise subclinical or hidden that drives the medical services envelope. So very similar profiles between the two with some small differences that I just mentioned.

<Q – Ekaterina Knyazkova – JPMorgan Securities LLC>: Thank you so much.

Operator: We'll move to our next question from Michael Ryskin with Bank of America. The floor is yours.

<Q – Mike Ryskin – BofA Securities, Inc.>: Great. Thanks for taking the question. Two quick ones for me. First, could you expand a little bit on what you saw in the quarter between wellness and clinical and especially as it touches on preventative care in the United States.

Just wondering if you're starting to see – or if you are seeing any separation there, just given the price increases between last year and this year and just thinking about willingness to spend, consumer sensitivity, if you're seeing any impact on demand from those side of things? And then I have a follow-up.

<A – Jay Mazelsky – IDEXX Laboratories, Inc.>: Yeah. Good morning, Mike. It's not unusual to see some variability in a given quarter between wellness and let's say, not wellness or sick patient visits. When you take a look at Q2 on a two-year basis, they were very similar growth profiles between the two, just small things that can account for some variability, whether more people are traveling, weather, what have you. What we tend to look at is we tend to look at those diagnostic parameters or menu that are used in wellness areas like 4Dx Plus, for example. And that was very strong growth. So we really haven't seen any drop off.

<Q – Mike Ryskin – BofA Securities, Inc.>: Okay. All right. Thanks. That's helpful. And then this is a little bit of looking ahead to 3Q, but just focusing specifically on international and Europe in particular. I know in prior years, you guys have seen occasionally a little bit of a headwind from weather, from extreme weather events, whether it's heat waves or hurricanes, et cetera, just because it would impact pet owner behavior or ability or willingness to visit the clinics, things like that.

Just thinking about the heat wave in Europe that's been going on for the last month or so. Is that factored into your guidance at all? Are you anticipating a little bit of an impact on revenues? I know you called out a days impact of modeling if there's any other wiggle room built in there for just the extreme weather? Thanks.

<A – Brian McKeon – IDEXX Laboratories, Inc.>: Yeah, Mike, I think weather at times can have impact on the business. Our outlook that I mentioned was that – for Q3 was organic revenue growth at the lower end of our full year outlook range. And that basically aligns with consistent strong execution trends and adjustments for the days effects. And just obviously, our pricing is evolving a bit here as well, so just compared to H1. So it's targeting consistent strong execution, and we'll address those types of impacts if they occur in the business and report on that if that turns out to be a factor.

<Q – Mike Ryskin – BofA Securities, Inc.>: All right. Thanks.

Operator: [Operator Instructions] We'll take our next question from Ryan Daniels with William Blair. Please go ahead.

<Q – Ryan Daniels – William Blair & Co. LLC>: Yeah. Good morning. Thanks for taking the questions. Just wanted to dive into the expansion of the US customer-facing organization a little bit more. I know it's been a while, and you've been more focused on OUS expansion. So can you talk a little bit about strategically what drove that? Is it just new clinic openings? Are you seeing more opportunities to visit vets? Is it kind of a competitive opening? Just any color there would be helpful.

<A – Jay Mazelsky – IDEXX Laboratories, Inc.>: Sure. So we've grown significantly in the US over the last years. I think it's been over three years since we did last expansion. We're very optimistic about the long-term growth prospects for the US. It's our largest market. It's something that we really evaluate on an ongoing basis. We want to make sure that we have the right account coverage, and we're able to support product and innovation priorities over time. So we felt that it made sense. It really just comes down to that.

<Q – Ryan Daniels – William Blair & Co. LLC>: Okay. Great. And then it's been a while since you've talked about a new big corporate win. And I'm curious if you could talk about maybe the competitive environment more broadly post some M&A activity in your space. Are you seeing that open up any opportunities or just normal course of business or more innovation? Thanks.

<A – Jay Mazelsky – IDEXX Laboratories, Inc.>: Yeah. I mean, I think the – it's really a normal course of business. We do very well with corporates. We occasionally talk about it. But from a corporate account standpoint, I think they see – increasingly see the integrated benefits of multi-modality solution and software. They're focused on workflow, and they're focused on productivity, given the capacity constraints and the need to really operate these models. And I think from a solution standpoint, they appreciate what we're able to bring. We have a footprint that's obviously very broad and deep and can work – can partner with them wherever they are. So I think it's a very natural fit from that standpoint.

<Q – Ryan Daniels – William Blair & Co. LLC>: Great. Thank you.

Operator: We'll move to our next question from Jon Block with Stifel. Please go ahead.

<Q – Jon Block – Stifel, Nicolaus & Co., Inc.>: Thanks, guys, and good morning. I'll break up my questions. Brian, it seems like the visits are expected to get a bit better in the second half of 2023. I think if I had it right, you mentioned flattish, give or take, year-over-year. But 2Q 2023 was down from the 1Q 2023 level.

So, maybe if you can elaborate a little bit on what helps the 2H 2023 visits from those first half levels? We did some work around labor constraints that might be easing a bit, but would love your thoughts on the improvement in 2H 2023. And then do we think about that trend line arguably continuing into 2024? And then I'll ask my follow-up.

<A – Brian McKeon – IDEXX Laboratories, Inc.>: Yeah. Thanks, Jon, for your question. I think the, A, part of it is working through this effect we saw in 2022, where there was a pullback in capacity. And so I think that pullback was largely happening in the first half of 2022. And so we knew we'd still be working through some of that. And I think that there'll be some relative improvement, which I think you were pointing out.

And I think, overall, we anticipate that we continue to look at the growth in demand that we see in terms of the expansion of the pet population and increased interest in pet health care, that being affirmed in a lot of the qualitative work that we do, believe that there's underserved demand and believe that that will be a positive tailwind over the long-term, continue to feel that's very much part of the growth build that we have for the long-term. And we're working through some dynamics here to help clinics adapt to that and improve their productivity, and I think we can be helpful.

So I think our long-term optimism is intact. That should be a positive driver over time, and we're – we've made some positive transitions here during the first part of this year.

I'd also highlight sometimes we spend a lot of time on the US trends that the – internationally, we've seen relatively more kind of same-store headwind effect that we've been able to offset with our benefits from our business expansion and engagement and innovations that we're bringing in.

And I think internationally, we see the same kind of a story that over time that there is very strong demand for pet health care. And it's probably relatively greater macro impacts in the near term, but we think that, over time, that will improve as well.

<Q – Jon Block – Stifel, Nicolaus & Co., Inc.>: Got it. That was very helpful. Thanks for that. And maybe just to pivot to innovation. When I look back to SediVue, I believe there was a staggered launch with the US leading and then international following. Any color on how we think of those pending new systems? Will we see sort of the same approach play out, the staggered call it?

And then, I don't know if you've talked about this before, but will the manufacturing be handled by yourself or your partners on those new systems? And just sorry, a quick clarifying question. Brian, I think price in the quarter, if I got you right, was closer to 9% for 2Q, but is full year 2023 price still expected to be between 7% to 8%? Thanks guys.

<A – Brian McKeon – IDEXX Laboratories, Inc.>: I'll let Jay dive into the platforms. On your latter question, yes, that's correct. That's what we said.

<A – Jay Mazelsky – IDEXX Laboratories, Inc.>: Yeah. So from a platform standpoint, I'm obviously not going to talk about it until we talk about it and get closer to the launch. What I will say, Jon, from a premium instrument placement and how we think about the opportunity, we typically do start with the US market, but there's nothing that says we have to do that. The key is really to build an installed base and get that consumable revenue stream moving.

That takes time. I think SediVue was one example. And we launched it, what, seven-plus years ago, and we built the installed base and we have a nice profile. So we really focus on being able to really drive sector development and adoption and solve those critical problems and everything else takes care of itself from there.

<Q – Jon Block – Stifel, Nicolaus & Co., Inc.>: Thanks, guys.

<A – Brian McKeon – IDEXX Laboratories, Inc.>: Thank you.

Operator: Our next question comes from David Westenberg with Piper Sandler. Please go ahead.

<Q – Dave Westenberg – Piper Sandler & Co.>: Hi. Thank you for taking the questions and congrats on continued strong execution here. So just a quick question, again, on that theme of pricing. I know that's one, well, a lot of people talk about. But maybe more on the clinic level, as we see continued constraints in labor, and that's really what we're seeing, are you seeing pressure from your customers to raise prices themselves? And do you think that's going to continue for, say, maybe the next six months or so? And do you see any kind of potential to maybe ease in volume as their prices go up? Or is it equilibrium as because maybe labor is used in a more optimal way?

And then just second, two really clarifying short questions. Can you just say how many territories you actually added? And then just on the gross margin commentary, you said – was it $18 million in terms of what the contribution was because of the hedge gains? I'm just trying to make sense of the 100 basis points of gross margin expansion. Thank you.

<A – Jay Mazelsky – IDEXX Laboratories, Inc.>: So quite a different question today. Let me just start with the price increase. Obviously clinics control that. If you go back, the last five or six quarters, a lot of clinics took multiple price increases on an annual basis. They typically – if you go pre-pandemic or pre-inflationary times, they would increase their prices onetime per year. I think a number of clinics on average increase at least two, in some cases, three. And that was really just to reflect the higher cost of labor and retaining staff. And in some cases, they need to add to staff.

And so from an employment level standpoint, we think clinics have – are catching up or caught up. They've hired people. That's not to say they're all working 40-hour weeks. And so in terms of pricing going forward, I think that's really just a reflection of what happens in the economy.

At this point, it appears that inflation has moderated somewhat, but we'll have to see how that plays out. And I think they'll make decisions based on how their businesses are doing. Right now, I think clinic revenue, practice revenue is pretty healthy for approaching 6% or so. So I think they feel like they're in a pretty good place from an economic standpoint.

<A – Brian McKeon – IDEXX Laboratories, Inc.>: And Dave, to your questions on gross margin and hedge gains, what we are trying to highlight is in terms of our year-over-year performance on margins that there is an effect in 2022 as the dollar was strengthening. We hedge out – we tend to hedge in advance of the year to help us with our planning.

And we had in the second half of last year, we recognized the benefit from $18 million in hedge gains. So what's happened with the foreign exchange dynamics is they've actually moved into a positive zone. So we have some benefit on revenue, but we're going to have some reported year-on-year foreign exchange headwinds.

We estimated 70, 80 basis points in H2 that relate to just lapping those hedge gains that will roll off eventually. So just trying to highlight that as a factor. We try to each quarter note what those gains or losses are. So you have that, and that's in our disclosures as well, so. But I just wanted to highlight that as you – to understand kind of the outlook.

<Q – Dave Westenberg – Piper Sandler & Co.>: Thank you for taking my long question.

Operator: Our last question comes from Balaji Prasad with Barclays. Please go ahead.

<Q – Mikaela Franceschina – Barclays Capital, Inc.>: Hi. This is Mikaela on for Balaji. Thanks for taking our questions. Can you talk about anything particular you saw in the quarter that drove the two-year stacked growth acceleration in CAG recurring? Thank you, so much.

<A – Jay Mazelsky – IDEXX Laboratories, Inc.>: Anything that drove the – was the question, anything that drove the two-year stack CAG Diagnostics recurring revenue growth?

<Q – Mikaela Franceschina – Barclays Capital, Inc.>: Yeah.

<A – Jay Mazelsky – IDEXX Laboratories, Inc.>: Okay. Yeah. I mean, the – as – we had a very strong quarter in terms of CAG Diagnostics recurred revenue, as indicated. It was really in part driven by pricing as well as volume growth and just really good execution. So retention of customers was very good. We saw adoption and utilization of diagnostics really across our broad spectrum. Obviously, consumables in our in-clinic business was very, very strong. And we saw nice performance in international, but that's really more of a cumulative impact of placements that we've, I think, achieved over the last four to six quarters.

<A – Brian McKeon – IDEXX Laboratories, Inc.>: Yeah. I'd highlight the two-year, I'm just looking at the numbers, on a two-year basis we have relatively consistent performance Q1 and Q2. So I think we had similar trends, similar benefits. And as Jay highlighted, I think we've had very good execution, including some benefits from the higher pricing this year.

Jonathan J. Mazelsky, President, Chief Executive Officer & Director, IDEXX Laboratories, Inc.

Okay. So with that, we'll conclude the Q&A portion of the call this morning. Thanks for everyone on the phone for your participation this morning. It's an honor to share another quarter of solid financial and strategic results as we continue to address a significant long-term opportunity to enhance standards of care for companion animals who are our unwavering focus on diagnostic insights. And so with that, we'll conclude the call. Hope to see you all at Investor Day, and thank you.

