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## **Johnson & Johnson's Management Discusses Q1 2013 Results - Earnings Call Transcript**

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Johnson & Johnson (NYSE:JNJ)

Q1 2013 Earnings Call

April 16, 2013 8:30 a.m. ET

### **Executives**

Louise Mehrotra – VP, IR

Dominic Caruso – VP, Finance and CFO

### **Analysts**

Matthew Dodds – Citigroup

Larry Biegelsen - Wells Fargo

Mike Weinstein - JPMorgan

Kristen Stewart – Deutsche Bank

Rajeev Jashnani - UBS

Derrick Sung - Sanford C. Bernstein

Tony Butler - Barclays Capital

Rick Wise - Stifel Nicolaus

Jami Rubin - Goldman Sachs

Danielle Antalffy - Leerink Swann

Matt Miksic - Piper Jaffray

## Operator

Good morning and welcome to the Johnson & Johnson First Quarter 2013 Earnings Conference Call. All participants will be able to listen-only until the question and answer session of the conference. This call is being recorded. (Operator Instructions) I would now like to turn the conference over to Johnson & Johnson. You may begin.

## Louise Mehrotra

Good morning and welcome. I'm Louise Mehrotra, Vice President of Investor Relations for Johnson & Johnson, and it is my pleasure this morning to review our business results for the first quarter of 2013. Joining me on the call today is Dominic Caruso, Vice President, Finance and Chief Financial Officer. A few logistics before we get into the details.

This review is being made available to a broader audience via webcast accessible through the Investor Relations' section of the Johnson & Johnson website. I'll begin by briefly reviewing highlights of the first quarter for the corporation and highlights for our three business segments. Following my remarks, Dominic will provide some additional commentary on the financial results and guidance for 2013. We will then open the call to your questions. We expect the call to last approximately 1 hour.

Included with the press release that was issued earlier this morning is the schedule of sales for key products and/or businesses to facilitate updating your model. These schedules are available on the Johnson & Johnson website as is the press release.

Before I get into the results, let me remind you that some of the statements made during this review may be considered forward-looking statements. The 10-K for the fiscal year 2012 identifies certain factors that could cause the company's actual results to differ materially from those projected in any forward-looking statements made today. The company does not undertake to update any forward-looking statements as a result of new information or future events or developments. The 10-K is available through the company or online.

During the review, non-GAAP financial measures are used to provide information pertinent to ongoing business performance. These non-GAAP financial measures should not be considered replacements for GAAP results. Tables reconciling these measures to the most comparable GAAP measures are available in the press release and on the Investor Relations' section of the Johnson & Johnson website at [investor.jnj.com](http://investor.jnj.com).

Now I would like to review our results for the first quarter of 2013. If you would refer to your copy of the press release, let's begin with the schedule titled, supplementary sales data by geographic area. Worldwide sales to customers were \$17.5 billion for the first quarter of 2013, up 8.5% as compared to the first quarter of 2012. On an operational basis sales were up 9.8% and currency had a negative impact of 1.3%. The acquisition of Synthes was completed in the second quarter of 2012. In the current quarter the acquisition, net of the impact of the divestiture of the legacy DePuy trauma business, contributed 5.7% to the worldwide operational sales growth.

In the U.S., sales were up 11.2%. In regions outside the U.S. our operational growth was 8.7% while the effect of currency exchange rates negatively impacted our reported results by 2.4 points. The Asia Pacific/Africa region grew 11.8% operationally while the western hemisphere excluding the U.S. grew by 9.1% operationally. Europe grew 6.2% on an operational basis. The success of new product launches and Synthes sales made strong contributions to the results in all regions.

If you'll now turn to the consolidated statements of earnings. Net earnings were \$3.5 billion compared to \$3.9 billion in the same period in 2012. Earnings per share were \$1.22 versus \$1.41 a year ago. Please direct your attention to the box section with the schedule where we have provided earnings adjusted to exclude special items.

As referenced in the accompanying table of non-GAAP measures 2013 first quarter net earnings were adjusted to exclude special items primarily related to an increase in the litigation accrual as well as integration and transaction costs related to the acquisition of Synthes, Inc. First quarter 2012 net earnings included a gain related to an after-tax special item of \$106 million as outlined in the reconciliation of non-GAAP financial measures. Excluding these special items for both periods, net earnings for the current quarter were \$4.1 billion and diluted earnings per share were \$1.44, representing increases of 8.0% and 5.1%, respectively, as compared to the same period in 2012.

I would now like to make some additional comments relative to the component leading to earnings before we move on to the segment highlights. For the first quarter of 2013, cost of goods sold at 31.7% was up 130 basis points from the same period last year, primarily due to an inventory step up charge related to the Synthes acquisition. Excluding the inventory step up charge which has been treated as a special item, cost of goods sold increased 50 basis points versus the same period last year.

Incremental amortization expense related to Synthes of approximately \$140 million negatively impacted cost of goods sold by 80 basis points. Also impacting cost of goods sold were the ongoing remediation work in our OTC business and the medical devices excise tax. Positive mix and cost reduction efforts partially offset these items.

First quarter selling, marketing and administrative expenses at 29.8% of sales were down 130 basis points due to tightening up expenditures as well as cost containment initiatives across many of our businesses.

Our investment in research and development as a percent of sales was 10.2%, consistent with our 2012 results.

Interest expense net of interest income of \$104 million was down \$26 million versus the first quarter of 2012 due to a lower average debt level. Other expense net of other income was \$515 million in the first quarter of 2013 compared to \$611 million of other income net of other expense in the same period last year. Excluding special items, other income net of other expense of \$83 million was \$411 million less than 2012 due primarily to lower gains from divestitures. Excluding special items, the effective tax rate of 19% in the first quarter of 2013 compared to 22.8% in the same period last year. Dominic will provide commentary on taxes in his remarks.

Turning now to business segment highlights, please refer to the supplementary sales schedule highlighting key products or businesses for the first quarter of 2013. I'll begin with the consumer segment.

Worldwide Consumer segments sales for the first quarter of 2013 of \$3.7 billion increased 2.2% as compared to the same period last year. On an operational basis, sales increased 3.3% while the impact of currency was negative 1.1%. U.S sales were up 2.4%, while international sales grew 3.8% on an operational basis.

Excluding the impact of divestitures net of acquisitions, operational growth was approximately 4.3%. Baby care products increased on an operational basis by 7% when compared to the first quarter of 2012 primarily due to wipes, hair care, cleansers and powders.

Sales in the oral care business increased 5.1% operationally. Results were driven by strong sales of LISTERINE due to the continued success of new product launches partially offset by the impact of the divestiture of the manual toothbrushes in the U.S.

For the first quarter of 2013, sales for OTC pharmaceuticals and nutritionals increased 7.6% on an operational basis compared to the same period in 2012, with U.S. sales up 14.4% and sales outside the U.S. up 3.9% on an operational basis. The strong sales results in the U.S. were driven by analgesics and upper respiratory products due to progress in returning to a reliable supply of products to the marketplace and a strong flu season.

Strong growth of analgesics drove results outside the U.S. Our skin care business was flat on an operational basis in the first quarter of 2013. Strong results for NEUTROGENA were offset by the impact of divestiture, the initial stocking related to new product launches last year and competitive pressure. Women's health grew 0.8% on an operational basis due to strong growth in liners offset by lower sales of KY products.

Wound Care/Other sales decreased 10% on an operational basis with the sales decline in the U.S. of 13.3% and outside the U.S. operational sales were down 6.1% due to competitive pressures and the impact of divestiture. That completes our review of the consumer segment and I will now review highlights for our pharmaceutical segment.

Worldwide net sales for the first quarter of \$6.8 billion increased 10.4% versus the same period last year. On an operational basis, sales increased 11.4% with the negative currency impact of 1 point. Sales in the U.S. increased 14.7% while sales outside the U.S. increased on an operational basis by 8.1%. U.S. results included a positive adjustment to previous estimates for managed Medicaid rebates under the Affordable Care Act related to new data received from the states. Excluding this item, both U.S. sales and worldwide sales were up approximately 8% operationally. The most significant impacts from the adjustment were in immunology, neuroscience and PROCRIIT.

Now reviewing sales for major therapeutic areas. Immunology products grew 16.8% operationally with sales in the U.S. up 12.8%. Excluding the adjustment, U.S. immunology growth was approximately 6.5% with REMICADE excluding export sales, up approximately 4%. SIMPONI up approximately 22%, and STELARA up approximately 57%. Results were driven by strong market growth across the major products, complemented by increased market share for STELARA. With the strength of our portfolio, we continue to be the U.S. market leader in immunology.

REMICADE exports sales declined 7.7% due primarily to a change in inventory levels. Immunology sales outside the U.S. increased by 30.1% operationally due to strong results for both SIMPONI and STELARA. SIMPONI's strong growth was due to the increased

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