Q2 FY22 Cardinal Health, Inc. Earnings Conference Call

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Operator: Good day, and welcome to the Cardinal Health Inc., Second Quarter Fiscal Year 2022 Earnings Conference Call. Today's conference is being recorded. At this time, I'd like to turn the conference over to Kevin Moran, Vice President of Investor Relations. Please go ahead.

Kevin Moran: Good morning, and welcome. Today, we will discuss Cardinal Health Second Quarter Fiscal 2022 results along with an update to our FY ‘22 outlook. You can find today's press release and presentation on the IR section of our website at ir.cardinalhealth.com. Joining me today are Mike Kaufmann, Chief Executive Officer, and Jason Hollar, Chief Financial Officer.

During the call, we will be making forward-looking statements. The matters addressed in the statements are subject to the risks and uncertainties that could cause actual results to differ materially from those projected or implied. Please refer to our SEC filings and the forward-looking statement slides at the beginning of our presentation for a description of these risks and uncertainties. Please note that during the discussion today, our comments will be on a non-GAAP basis unless they are specifically called out as GAAP. GAAP to non-GAAP reconciliation for all relevant periods can be found in the schedules attached to our press release.

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

Mike Kaufmann: Thanks, Kevin, and good morning, everyone. Today, Jason's and my comments will be consistent with the update we provided a few weeks ago. Let me start with a few high-level thoughts.

At an enterprise level, we continue to focus our efforts on 3 strategic priorities: optimizing our core businesses, investing for growth, and innovation, and deploying capital efficiently. We continue to believe the long-term targets we announced in November are appropriate. And, we remain on track to meet our $750 million enterprise cost savings target by FY ‘23.

Our Pharma business is performing as planned. We've seen volumes continue to improve sequentially, and we are encouraged by the growth we saw again in Q2. Looking ahead, we continue to expect Pharma to realize mid-single digit growth in FY ‘22.

In our Medical segment, we continue to experience unprecedented inflationary impacts and global supply chain constraints in our core US Medical and Products Distribution business. These impacts, combined with lower-than-expected offsets from pricing actions, will significantly impact Medical segment profit consistent with our update a few weeks ago.

While we believe these impacts are temporary, the timing of when they will abate remains difficult to predict. Consequently, we are urgently working to mitigate the effect of these external macroeconomic challenges on our business.

We are seeing progress in other areas of the Medical segment, including our lab business in growth areas, and we recently extended several key acute care distribution customers. Looking ahead, I'll elaborate on the actions we are taking to drive performance, particularly for Medical, after Jason reviews our Q2 results and updated outlook.

Jason Hollar: Thanks Mike, and good morning, everyone.

Beginning with total company results, second quarter revenue increased 9% to $45 billion, driven by sales growth from existing Pharma customers. Total gross margin was $1.6 billion, a decrease of 9% primarily due to the Cordis divestiture and elevated supply chain costs in Medical.

Consolidated SG&A was flat to the prior year at $1.2 billion, as the Cordis divestiture and benefits from cost saving initiatives offset IT investments and higher operations expenses.

Second quarter operating earnings were $467 million. Outside of the incremental inflationary impacts in Medical, these results were generally in line with our expectations.

Moving below line, Interest and Other decreased by 30% to $24 million, driven primarily by lower interest expense from debt reduction actions.

Our second quarter effective tax rate finished at 19.4%, six percentage points higher than the prior year due to certain discreet items, which primarily benefited the prior year period. Additionally, our second quarter rate this year included some timing favorability.

Average diluted shares outstanding were 281 million, 5% lower than the prior year due to share purchases. Of note, we initiated a $300 million share repurchase program in the quarter, which was recently completed and brings our total year-to-date repurchases to $800 million.

The net result for the quarter was EPS of $1.27.

Second quarter operating cashflow was strong at $1.2 billion. As a reminder, the day of the week in which the quarter ends affects point-in-time cash flows. We ended the quarter with a cash balance of $3.2 billion and no outstanding borrowings under our credit facilities.

In the quarter, we also recorded a $1.3 billion non-cash, pre-tax goodwill impairment charge related to the Medical segment, which is excluded from our non-GAAP results. This accounting charge primarily resulted from additional inflationary impacts and global supply chain constraints I will discuss shortly.

Now turning to segments, beginning with Pharma on slide 5…

Revenue increased 11% to $41 billion, driven primarily by branded pharmaceutical sales growth from large Pharmaceutical Distribution and Specialty customers.

Segment profit increased 3% to $426 million driven by generics program performance. This was partially offset by our previously discussed investments in technology enhancements and higher operations expenses, including cost supporting sales growth, such as transportation and labor.

During the quarter, we were encouraged to seek continued, broad-based improvements in pharmaceutical demand consistent with our expectations, including a return of generics volumes to approximately pre-pandemic levels. Our generics program continued to experience generally consistent market dynamics, including continued strong performance from Red Oak. Outside of generics, we've seen brand inflation trending in line with our expectations.

Turning to Medical on slide 6…

Second-quarter revenue decreased 5% to $4.1 billion, primarily due to the divestiture of the Cordis business.

Segment profit decreased 79% to $50 million, primarily due to inflationary impacts and global supply chain constraints in products and distribution. This also reflects the timing of selling higher cost PPE, including the net positive impact from this dynamic in the prior year, and to a lesser extent, the divestiture of the Cordis business.

During the quarter, our products and distribution business continued to be impacted by significant inflationary pressures in the global supply chain, primarily in the areas of polypropylene and international freight. Additionally, in the quarter we saw broader inflationary impacts across the business such as domestic freight and other commodities, as well as global supply chain constraints affecting the volume of some of our higher margin Cardinal Health brand products.

I'll discuss these impacts with respect to our full year Medical outlook momentarily, and Mike will elaborate on the actions we are taking to address these macro challenges and drive performance in our core Medical business.

With respect to COVID-19 and the Omicron variant, we continue to see strong performance from our Lab business, including significant testing demand generally consistent with level seen a year ago. And, despite some impacts from Omicron in various geographies, demand for surgical products related to elective procedures was comparable to both the first quarter and prior year.

Now, transitioning to our updated fiscal 22 outlook on slide 8…

We now expect EPS in the range of $5.15 to $5.50 per share, primarily reflecting our updated expectations for Medical. We also now expect an annual effective tax rate in the range of 23% to 24.5%, and Interest and Other in the range of $140 to $160 million, with the improvement in I&O including deferred compensation favorability which, as a reminder, is fully offset above line in corporate SG&A.

As for the segments on slide 9…

For Pharma, no changes to our outlook. We continue to expect low-double digit revenue growth and mid-single digit segment profit growth.

For Medical, we now expect revenue to be down low-single to mid-single digits and segment profits to be down 30% to 45%.

Consistent with the financial update provided a few weeks ago, we expect increased inflationary impacts and global supply chain constraints, as well as lower-than-expected pricing offsets, to result in an estimated incremental $150 to $175 million headwind to Medical segment profit for the full year. This, in addition to our November 9th update regarding the pressures in international freight and polypropylene, now reflects a total net incremental headwind of approximately $250 to $300 million to Medical in fiscal ‘22. While these impacts have persisted for longer than previously anticipated, we continue to believe the majority will be temporary as global supply chain pressures eventually abate. While it will take time, we are committed to mitigating the impacts of inflationary pressures, and will continue to work through these dynamics with our customers.

Now, a few other things to keep in mind in terms of the fiscal ‘22 cadence…

For Pharma, we expect the year-over-year growth in the back half to be heavily weighted to the fourth quarter due to the lapping of some prior year items, including higher costs for the deployment of IT investments, and the general sequencing of our growth initiatives.

In Medical, we continue to expect an unfavorable year-over-year impact due to timing of selling higher cost PPE in the second half of fiscal ‘22, though not to same magnitude as in the second quarter. We also will be lapping the large prior year PPE inventory reserve in the fourth quarter.

Finally, to close, a few reminders on capital deployment…

We continue to expect to pay down the approximate $280 million of remaining June 2022 notes at maturity, and continue to expect approximately $1 billion in total share repurchases in fiscal ‘22.

As we’ve said, we see our increasing balance sheet flexibility supporting more opportunistic return of capital to shareholders as our debt paydown begins to moderate, enabled by our recent $3 billion share repurchase authorization.

We continue to believe that capital deployment, along with the future growth that we expect in both our segments, will drive the long-term, double-digit combined EPS growth and dividend yield that we are targeting.

With that, I’ll turn it back over to Mike.

Mike Kaufmann: Thanks, Jason.

In Medical, we're continuing to take action to drive performance and maximize the differentiated strengths we have in this business. We are vertically integrated with distribution through our comprehensive Medical products portfolio, which is generally oriented around the Operating Room and the Intensive Care Unit. We also have an advantaged Lab products portfolio and higher margin growth businesses. With our diverse customer base, we cross-sell products and services spanning our portfolio.

To address the challenges in our Medical business, we're focused on 3 things:

First, evolving our commercial contracting strategies and driving mix. Historically, costs have been relatively stable and industry participants have committed to longer-term, multi-year contracts. However, the rapid escalation of today's inflationary pressures demonstrate that our contracting strategy needs to change. We are in the process of working with our customers to adjust certain contracts to ensure we have more pricing flexibility for factors beyond our control.

With regards to mix, as I noted in the prior quarter, we have made important changes to align our commercial organization's structure and incentives. We are under-penetrated in Cardinal Health brand mix relative to our potential, which remains a significant mid to long term profit opportunity as we move past the pandemic and associated supply chain challenges.

Within our Medical products portfolio, we are actively improving our key category product offerings. For example, in our Incontinence product line we have launched a new Cardinal Health brand stretch brief and a comprehensive breathable platform. These enhancements directly support and meet our customers' needs.

Second, we are simplifying our operating model, and optimizing our international footprint.

We remain on track regarding the timing of the previously-announced exits in certain commercial markets, with 35 of the 36 completed to-date.

We are also focused on the modernization of our distribution facilities, including breaking ground on a new distribution center in the Midwest with nearly triple the space of the existing facility enabling future growth.

We believe that a diverse, global sourcing network is important to remain competitive on cost, and are investing in additional self-manufacturing capabilities, including increases in annual production of safety needles and syringes, isolation gowns, and surgical and procedure masks in our own North American facilities. Specifically for surgical gowns, we have efforts underway that will double our North American finished goods production and enhance our supply chain resiliency.

Third, we continue to invest across the Medical segment, including in our growth businesses, at-Home Solutions and Medical Services, which are aligned with industry trends and positioned to grow double-digits in FY '22 and beyond.

In at-Home Solutions, we continue to see strong demand as care continues to shift into the home. We recently announced an additional strategic investment in Medically Home, a technology company that enables health systems and other partners, like Cardinal Health, to safely bring the hospital home, where patients increasingly prefer to receive their care. Not only does this hospital at home model benefit patients, it also provides needed capacity for hospitals and delivers care in a lower cost setting.

And in our higher-margin Medical Services businesses OptiFreight® Logistics and WaveMark, we continue to enable clinically integrated and digitally automated supply chains, and are seeing growth driven by an expanded customer base and diversified solutions. We've invested in additional technology capabilities to increase our offerings in both businesses. In OptiFreight®, we've invested in additional technology capabilities focused on building automated, technology-driven solutions that innovate the way healthcare supply chain leaders manage shipping spend and take control over their transportation logistics. These efforts are connecting suppliers and customers at over 22,000 shipping locations.

In WaveMark™, we launched a cutting-edge supply automation solution for clinical labs, which automates previously manual inventory management tasks. This enables clinical lab staff to focus on patient care and better manage increased testing demand due to COVID-19.

Our Pharma business remains on track to deliver mid-single digit growth in FY '22. We continue to make progress on our 2 primary objectives:

First, strengthening our core Pharma Distribution, or PD, business. This quarter's segment profit was driven by the performance in our generics program. Our generics program is anchored by the scale and expertise of Red Oak Sourcing, a partnership we also recently extended through FY '29, and which positions us well to meet customers' needs. In addition, our multi-year technology investment to modernize our systems is on track. We plan to complete the roll-out by the beginning of our Q4 and look to benefit from the conversion in FY '23 and beyond.

Second, we're fueling our growth businesses: Specialty, Nuclear, and Outcomes.

In Specialty, we continue to experience momentum in our oncology physician office business, driven in part by Navista TS, our technology platform for value-based care. Just this week, we announced a partnership with Ember Technologies to offer the world's first self-refrigerated, cloud-based shipping box for temperature-sensitive medicines. As Biopharma continues bringing cold-chain biologic products to market, including cell and gene therapies, this partnership will help ensure product integrity throughout the supply chain. This is a differentiated offering, and one that will reduce landfill waste by millions of pounds annually. And with biosimilars, we are well positioned to support the next phase of growth as biosimilars expand into new therapeutic areas and sites of care.

In Nuclear, we expect continued double digit profit growth, which would result in a doubling of our profits in this business by FY '26. We continue to build out our multimillion-dollar Center for Theranostics Advancement in Indianapolis, where we've partnered with several pharma companies to develop and commercialize novel theranostics, and we're investing in our PET capabilities to support robust PET diagnostics. For example, with the FDA approval of Telix's radiopharmaceutical in Q2, we are positioned to drive nationwide accessibility and broad adoption of prostate-specific PET imaging for physicians and eligible patients across the United States.

And in Outcomes, we are adding new payers and PBMs and expanding clinical solutions for both independent pharmacies and retail chains. Outcomes recently activated its 20 millionth user on its digital patient engagement platform, which enables two-way communication between pharmacies and patients to increase medication adherence.

With respect to the Enterprise, we continue to aggressively review our cost structure as we work to streamline, simplify and strengthen our operations and execute our digital transformation. We're pairing cost reduction efforts with balanced, disciplined, and shareholder-friendly capital allocation with a focus on investing in the business, maintaining a strong balance sheet and returning cash to shareholders. Long term, we're targeting a double-digit combined EPS growth and dividend yield. These expectations are driven by our growth targets for our segments, our commitment to our dividend, and our $3 billion share repurchase authorization.

Now, let me provide an update on the proposed opioid settlement agreement and settlement process.

As of today, 46 out of 49 States have indicated their intent to join the global settlement.

The sign-on period for political subdivisions within participating states concluded on January 26th. Now, each of the participating states are in the process of determining whether there is sufficient subdivision participation to proceed. After we receive notice from the states regarding their decision, each of the distributors will make final determinations by February 25th.

If all conditions are satisfied, this agreement would result in the settlement of a substantial majority of opioid lawsuits filed by the state and local governmental entities. This is an important step forward for our company. As we've consistently said, we remain committed to being part of the solution to the U.S. opioid epidemic and believe that settlement would provide relief for our communities and increased certainty for our shareholders.

In closing, our aspiration has been and continues to be that we are healthcare's most trusted partner. We will do this by focusing on our customer's needs and delivering the products and solutions that advance healthcare and improve the lives of people every day. We bring life-changing healthcare innovation to market, harnessing the power of technology, data and insights to optimize care delivery. We're investing in technology and analytics to drive future growth in evolving areas of healthcare and address healthcare's most complicated challenges.

What we do matters. And we're focusing our resources on building solutions to meet the needs of our customers and their patients, now and in the future.

And now, Jason and I will take your questions.

Operator: Thank you.

And if you would like to ask a question, please signal by pressing star 1 on your telephone keypad. If you're using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment.

And we'll go ahead and take our first question from Charles Rhyee, with Cowen and Company. Please, go ahead.

Charles Rhyee: Yeah. Thanks, guys. Mike and Jason, I want to talk about the issues with supply costs here and we're obviously challenged at the moment, but can you talk a little bit more about as let's say these pressures ease, let's say hopefully later this year or whenever, can you talk about how those expenses that you are incurring today roll off. Do they kind of roll off fairly quickly, or is it that it these kind of knock on effects of delays and everything for all your supplies and equipment. Just kind of just drag even further beyond if we were to see reports that, Hey, the ports are working as normal. How long is that kind of follow-on effects before everything really would return to normal? And from a P&L perspective, do the - are these kind of expenses kind of overshadowing, let's say sort of the underlying performance of the division or - a little more color on that would be helpful. Thank you.

Jason Hollar: Sure. I'll definitely start here, Jason, and then I'm sure Mike will have some thoughts as well. But generally speaking, the vast majority of these costs that we've outlined are product-related costs or costs to get the products shipped to the United States where our customers typically are. And as such, most of those costs are included in inventory and then expensed as they're sold. So that means that there would be a one to two quarter delay in terms of when those costs begin to come down, and when you would start to see that offset then in the P&L. And that's I think, fairly typical for the - what we saw with PPE as well last year in terms of that type of cadence.

Now there's - some of this, a smaller portion is related to the volume impacts of the supply chain constraint. So that's obviously going to be at the time that volume frees up. There's a small part that's a period cost, but it's much less significant. Again, the biggest buckets when you step back and think about the $250 to $300 million that's in aggregate that we're talking about, it's that international freight is the biggest piece and is very much inventoried as I just described. And then the second largest would be the general commodities we've talked about. Commodities like oil-based commodities like polypropylene. That is a big driver. That again, those would all the inventoried costs and then flowing through.

As it relates to the overall impact to the business, just using Q2 as the example from a year-over-year perspective, this overall aggregate impact of the inflation and net of pricing is the greatest driver that year-over-year reduction. We did as a reminder have favorability last Q2 as it relates to the timing of PPE pricing cost. So there's a little bit of a headwind on an absolute basis this quarter, but it's more significant the comparison to the favorability of last year. And that's about $60 million in this quarter, so that's a relevant piece to the year-over-year impact. And then the final piece, as you know, Cordis is running at roughly last year was roughly $20 million a quarter. So the absence of that business as was divested is that last piece. So I think that gives you most of the key pieces.

Mike Kaufmann: Yeah. The only thing I would add, Charles, is that, while everything Jason said is true, the one, the two quarters and all that, one thing I want to make sure people understand is, we're actively getting after this now. So we're not going to have a strategy of just waiting for these to come down. So we are evolving our commercial and contracting strategies. That is something we're actively doing. Working with customers to be able to either pass on some of these prices, change our contracting, driving our mix as we talked about, and continuing to aggressively get after our cost and invest in our growth businesses. So, while we will hopefully see these come down because we do believe these are temporary, we're also at the same time getting after things that we need to do to manage to operate the business aggressively. Next question.

Operator: And we'll go ahead and move on to our next question now from Lisa Gill with J.P. Morgan. Please go ahead.

Lisa: Thanks very much. Mike, can I just first start with just a follow-up to what you just talked about. When we think about your Medical business longer-term, I know you previously had a goal of north of 5% operating margin for med surge. I know they - part of that was the higher margin of Cordis, but when we get back to a more normalized basis, how do we think about what the margin should look like in that business?

Mike Kaufmann: Yeah. You know, it's a great question. We've not put that out there. I will give you a couple things. Obviously, as the inflation goes away, and as we said we believe this $250 to $300, the vast majority of that is temporary, so you can add that back to our margin rates as the biggest driver. Second of all, the second thing I would add, is we said we want to drive mix. And what we mean by that is selling more of Cardinal Health branded products versus national brand. That's going to also drive our mix in a positive way. We're getting after expenses. That's going to - I'm sorry - that's going to drive our margins too for the segment. And we're growing our growth business, which do have higher margins. So all of our key initiatives not only will drive bottom line, but they all should drive margin rates up significantly. But at this point in time, we've not put a target margin rate out there that we're going after.

Operator: And we'll go ahead and move on our next question from Eric Percher with Nephron Research. Please go ahead.

Eric Percher: Thank you. I want to stay on this topic. And my question is, can we talk a little bit about your expectations for some of these specific items maybe built into the year or your view on duration. And I separate freight commodity and then the sales volume and duration on how long you pass this on given the new contracting methodology. Can you just give us your take on either expectations today or based on prior experience in what you know today, the duration of those pressures.

Jason Hollar: Yeah. Again, this is Jason. I'll start. So to your point, it will potentially differ, not only by type of cost, but also the magnitude of what we're talking about. So as it relates to first of all, just the international freight, one thing to highlight is that particular area of cost has remained at very elevated levels. So at this point, we're not seeing much of a change from where we have been. And so that's something that is a clear part of our pricing focuses to make sure we can get at least a good portion of that recovered. As it relates to some of the other commodities, they've been more volatile. We have seen some that have started to appear to come down that cost of. It looks like they may have plateaued and started to reduce others that have been choppier. And so in that environment where the costs are moving around a lot it is - provides more challenges as it relates to getting that pricing more established.

I think the key is, as you think about the cadence of what this impact is on a net basis that $250 to $300 million, we have already incurred about $100 million of that year-to-date. That $150 to $200 million that's remaining within our guidance, we see that peaking in the third quarter, and that's a combination of not only the costs we expect to be at it's highest. And then as they start to come down and it takes that delay to get it actually flowing through our inventory to our P&L, that then we'll start to benefit us later in the year. But also, that's also the timing of when we would start to see some of the pricing actions that we have already begun to start to come through.

It is just the beginning. It's not offsetting enough of that. And there's more activity that will need to still occur, but it all depends on exactly what that cadence is of cost. And the key is that we remain very close to both the GPOs, as well as our customers, to manage through that on an item-by-item, customer-customer basis to get to an answer then that would give us the right cadence exiting the year. With all that said, given the one to two quarter lag even if costs do come down and even if we have more success with the pricing, we would expect there to be a carryover into fiscal ‘23. There will be some impact that carries over into that year, but we need to see the cadence of both the cost and the pricing before we can establish that more clearly.

Operator: I'll go ahead and move on to our next question from Ricky Goldwasser with Morgan Stanley. Please go ahead.

Dan: Hi, good morning. This is Dan on for Ricky. Two questions from us. One, as we think about your move to move more finished goods production back to North America, how should we think about that in terms of margin, both sort of in a pre-COVID environment and then the impact to margin as we think about your margins in recent quarters. And then as a follow-up just wanted to confirm, was the updated tax rate interest expense guidance that came out today, was that included in the early January update or is that incremental? Thank you.

Mike Kaufmann: I'll have Jason talk about the tax rate and then I can talk about the margin.

Jason Hollar: Yeah. And so the - there were some small differences in this latest update. The tax rate was just bringing down the top end a little bit, the low end was the same, so it's not much of a difference there. The Interest and Other change I highlighted was in part related to deferred comp. And as a reminder, that's just geography between Interest and Other as well as corporate SG&A. So yes, it was largely considered in our prior assumptions, but as a lot of it was just geography, anyway, so there's no material difference in those other updates.

Mike Kaufmann: And as far as moving capacity to North, you know, to our North American operations, I would say a couple things. Generally, I wouldn't say that we would expect much of a margin difference if it was manufactured outside of North America versus manufactured here. That is not something I would say would be a margin driver. It's more about supply chain integrity, which is why we've moved them there. So if there are disruptions in the future, we obviously then have certain key items closer here. So we've chosen these items that can be highly automated, make a lot of sense, and freight is a big piece of it so that we can still stay cost competitive. So again, wouldn't say it's margin generating in and of itself. However, by increasing the capacity on some of these items, like we mentioned, doubling our ability to manufacture our own gowns, that does give us more ability to sell our own product, which as we drive mix, that would increase our overall margin rate.

Operator: And we'll move on to our next question from Jailendra Singh with Credit Suisse. Please go ahead.

Jailendra Singh: Thank you, and good morning, everyone. With respect to this 250 to 300 million impact in Medical segment, can you be a little bit more specific on how much impact did you see in fiscal first half and how much is expected in second half. And a follow-up to an earlier question, how should we model the split between 3Q and 4Q on the remaining impact. Trying to better understand if all these initiatives you're put in place are more focused on policing the company better next time you see these kind of pressure, or do you think there's a possibility these initiatives result in some near-term offset, and are you capturing those in your outlook?

Jason Hollar: Yeah, if I understood the question right, Jailendra, the - I think I'd answered before, but I'll go and repeat that. So the $250 to $300, $100 million was - has already been incurred in the first half. Think about it as kind of a sequential step up. So Q2 is higher than Q1 and Q3 is expected to be higher than Q2, and then it - then that's the period it peaks before it starts to come back down. So there's - depends on if we're talking sequential or year-over-year. From a sequential perspective from Q2 to Q3, within the Medical business there's just the ongoing cost that we would expect to be always in place, that continue. Those initiatives we've talked fairly consistently about are there. Within the other type of PPE impacts, like I said from a year-to-year perspective in the second quarter, it was $60 million headwind. There was a small headwind in an absolute basis in the second quarter that we think will be less in the third quarter, so that's a bit of an offset, not significant. But generally speaking, it's the inflationary impact. So the most pronounced from a year-to-year, as well as expected to be a little bit greater than in the third quarter.

Mike Kaufmann: The things I would add to be helpful here is, as Jason mentioned, as we expect some of the inflation impacts to start to hopefully come down some, and that'll give us a little bit of benefit in Q4. We also see our pricing actions ramping up some in Q4 too, because we are continuing to implement additional pricing actions. We have some going into effect here very soon, that have been agreed to, so we're working through those. So I would say that that would be a positive item going forward for us. Also, as we mentioned, are working on our commercial contracting strategies. And so as we work through those contracts, our goal is to give us more flexibility so that in the future, if there is another instance like this, we are able to react quicker and address our pricing and work with our partners in a very transparent and productive way. Because our customers are obviously something that we have to always have in the front of our mind. But we do need some more flexibility in the business, and we are working aggressively to work with the GPOs and our customers to do that.

Jason Hollar: And Jailendra as you do your modeling for the balance year, just remember in the prior year, we had a significant inventory charge in Q4 that would, of course, not be expected to replicate here this year.

Operator: And we'll go ahead and move on to our next question from Michael Cherny with Bank of America. Please go ahead.

Michael Cherny: Good morning. Thanks for the details. Mike, you mentioned your remarks how you had a few customer extensions with some of your key customers on the Medical side. Especially against this backdrop of your focus on recontracting, would love to know a little more detail about how qualitatively those discussions went in terms of your thought presses about recontracting, were you able to test out? What you were able to get through and not get through, and what customers were willing to accept relative to that change contracting dynamic, especially given that these are obviously extensions on customers that have worked with you, I assume, for at least a long time.

Mike Kaufmann: That's a great question. Yeah, we are working aggressively on that. It's not just the individual customers. In fact, it's just as important to be able to work with our GPO partners to allow us, because you really have to coordinate between all three of them. So there's still absolutely work to do, but we're seeing some positive signs from both the GPOs and the customers that understand the importance of having a strong supply chain and strong supply chain partners in the - in Medical distribution, that these are things that we're going to have to work together. Key things that we've learned through those discussions that will be helpful is, one, a willingness to be transparent with them so that they understand as costs come up, why are they going up? But also when costs come down so that they know that you're not continuing to charge a high price when things have got better. And we're very willing to work with them on this transparency piece, which I think will help both parties understand the importance of what we need to do here from a pricing standpoint. So I would say early indications have been positive, but still a lot of work to do as we work on changing our commercial strategies.

Operator: And our last question comes from Elizabeth Anderson with Evercore. Please go ahead.

Elizabeth Anderson: Hi guys. Thanks so much for the question. I was wondering if you could comment on, as we sort of have gone through a month of the new quarter, just how you're seeing sort of volumes come back. Particularly on the surgical side and also on sort of home care, just to sort of we think about the cadence for that going through the back half of the year.

Jason Hollar: Yeah. And maybe I'll just take the opportunity to talk about volumes in general because it - I think whether it's Pharma or Medical, the general response is about the same. Within Medical, while there's been certain level of choppiness over the last three, six months, largely it's been very consistent with our expectations. We indicated before we are back to near pre-COVID levels. And this quarter was pretty consistent with our expectations, and sequentially, from the first quarter as well as year-over-year, there were not many differences. And so there's noise, but the key is that state-by-state, geography-by-geography different regions are impacted at different times to different extent, but we're just not seeing big impacts. And that's because our customers continue to do a wonderful job of providing great service to their patients. And that's providing a better balance underneath the volume than what we saw earlier on in the pandemic.

On the Pharma side, we continued to talk in today's prepared remarks, as well as a couple weeks ago, just that we continue to see that widespread improvement back to pre-COVID levels. And we have largely gotten back to that point at the end of the second quarter. And so we're just not seeing a lot of variability there as well.

Operator: And with that, that does conclude our question-and-answer session for today. I would now like to turn the call back over to Mike Kaufmann for closing remarks.

Mike Kaufmann: Thanks, Allie. I want to thank everybody for taking the time to be on the call today, and for all of your questions. I'd like to conclude by reiterating that we are taking action to mitigate these inflationary impacts and supply chain constraints, and we're laser-focused on driving improved performance across all of our businesses. So please stay safe, and we'll speak with you again soon. Take care everybody.

Operator: And with that, that does conclude today's call. Thank you for participation. You may now disconnect.