Microsoft accelerates industry cloud strategy for healthcare with the acquisition of Nuance

Company Participants

- Amy Hood, Chief Financial Officer
- Mark Benjamin, Chief Executive Officer
- Satya Nadella, Chief Executive Officer
- Scott Guthrie, EVP of Cloud & AI

Presentation

Operator

Good morning. Thank you for joining us for the conference call regarding Microsoft's Acquisition of Nuance. On the call with us today are Satya Nadella, Chief Executive Officer of Microsoft; Mark Benjamin, Chief Executive Officer of Nuance; Amy Hood, Chief Financial Officer of Microsoft and Scott Guthrie, Executive Vice President of Cloud and AI of Microsoft.

Today's call is being webcast live and recorded. You can replay the webcast as well as view the prepared remarks and supplementary slide deck on the Microsoft Investor Relations website following the call. During this call we will make forward-looking statements, which are predictions, projections or other statements about future events. These statements are based on current expectations and assumptions that are subject to risks and uncertainties. Actual results could differ materially because of factors discussed in today's press release and presentation and comments made during this call and in the Risk Factors section of our Form 10-K, Form 10-Q and other reports and filings with the Securities and Exchange Commission. We do not undertake any duty to update any forward-looking statement.

And with that, I'll turn the call over to Satya.

Satya Nadella {BIO 3224315 <GO>}

Thank you, Brett. And thank you, everyone, for joining us this morning to talk about this very exciting announcement. I want to briefly discuss what this acquisition will mean for both Microsoft and for Nuance.

For us, everything starts with our mission to empower every person in every organization on the planet to achieve more. Microsoft and Nuance both share a passion for ensuring people everywhere and the institutions they build are benefiting from the latest advances in digital technology. We are both partner-first

companies and are deeply committed to building ecosystems to ensure customers have complete solutions they need to address their unique challenges. Together with our partners, we will put advanced AI solutions into the hands of professionals to drive better decision-making and create more meaningful human connections.

First and foremost, this coming together is about empowering health care. It's about applying the technology, talent, industry expertise and partner mindset of our two companies to this very critical industry in order to empower everyone from ISVs to EHR vendors, to physicians, nurses and, of course, patients.

Coming out of the pandemic, we are experiencing digital transformation at a scale never seen before. Entire industries are being reimagined in mere months. This is driving lasting structural change and accelerating digital transformation driven by industry-specific cloud solutions.

It's now very clear that healthcare organizations that accelerate their digital investments can improve patient outcomes and reduce costs at scale. Advances such as AI will have an enormous impact on augmenting human capability in healthcare. AI is technology's most important priority, and healthcare is its most urgent application.

That's why we are so energized by today's announcement. Nuance is a pioneer in enterprise AI, and it's the AI layer at the healthcare point of delivery. Nuance created the voice recognition category more than 20 years ago. Its technology is deeply integrated with solutions, medical professionals use all day every day. 77% of US hospitals are Nuance customers. Three out of four radiologists in the United States use Nuance to improve their effectiveness. And more broadly, 85% of the Fortune 100 use Nuance, applying AI to connect with their customers in new ways and protect them with advanced biometric security.

Nuance has great momentum in cloud and AI first solutions in three key areas. First, ambient clinical intelligence. Nuance's Dragon Ambient eXperience solution has completely redefined clinical documentation by capturing and contextualizing every word of the physician/patient encounter and automatically documenting it in the EHR. Deep learning securely converts conversations into structured notes tailored to each medical specialty. This clinical documentation essentially writes itself, giving physicians time back to focus on patient care. It's a fantastic example of how AI and cloud computing are being embedded in the world today, whilst preserving trust, security and privacy. This is projected to be one of the fastest-growing infrastructure software revenue streams in history.

Second, healthcare cloud. More broadly through its integrations with core healthcare systems like EHR, Nuance is moving key workflows in radiology, healthcare, speech recognition and medical coding to the cloud, reducing the burden on clinicians and delivering better clinical and financial outcomes. For example, Nuance is creating powerful feedback loops across the entire AI layer, connecting workflows, care pathways, quality reviews and EHR integrations to support critical clinical decision

making. Think of this as an AI learning loop for continuous improvement for every provider.

And finally, cross-industry enterprise AI, specifically customer engagement and biometric security. Nuance is building the next-generation omni-channel customer engagement cloud service at a time when every business is re-imagining how it interacts with customers. Nuance is also applying AI to security with biometric security solutions to authenticate customers and prevent fraud. 8 billion authentications are enabled by Nuance's biometric services annually, and 31 billion customer interactions flow through their solutions each year.

Today, the Microsoft Cloud is differentiated and is leading with industry and cross-industry solutions and our opportunity is to take Nuance's momentum and add Microsoft Cloud for Healthcare. Six months ago, we introduced the Microsoft Cloud for Healthcare, which brings together the breadth of our offerings and adds new capabilities, customizations and standards unique to the industry. Nuance and Microsoft complete the end-to-end patient-provider workflow, capturing the patient interaction, converting into clinical documentation and conducting follow-up actions.

Together, Nuance's momentum and growth in these key areas, paired with Microsoft's scale across the enterprise, will increase our total addressable market and expand our AI leadership. Nuance will double our TAM in healthcare provider space and increase our TAM across healthcare to nearly $500 billion [ph]. This acquisition brings our technology directly into the physician/patient loop, which is central to all healthcare delivery.

The acquisition will also expand our leadership in cross-industry enterprise AI and biometric security. Nuance is a recognized leader in conversational AI for intelligent customer engagement through interactive voice response, virtual assistants and voice biometrics. Most importantly, together, we will drive increased customer benefits by augmenting the Microsoft Cloud for Healthcare with Nuance and by combining Nuance's deep enterprise AI expertise with the Microsoft Cloud, we will deliver powerful next-generation services and accelerate the growth of Nuance's business and drive growth across our complete tech stack.

I'm greatly looking forward to empowering our customers together and the new opportunities we will create with them. To share more, I will turn it over to Nuance's CEO, Mark Benjamin. Mark?

Mark Benjamin {BIO 16617270 <GO>}

Thank you, Satya. At Nuance, we focus on creating intelligent solutions that amplify our customers' ability to help others [ph]. From revolutionizing the doctor-patient relationship to reinventing the way large organizations connect with their customers, Nuance is a leader in conversational AI and ambient clinical intelligence. We have pioneered speech technologies, natural language understanding and machine learning for more than 20 years. So AI is certainly in our DNA.

Over the past three years, we've gone through a transformation to streamline our portfolio, transition to the cloud, and reinvigorate our purpose around healthcare and enterprise AI to deliver solutions that shape the future of work and care. We are redefining how work gets done in these areas, making our customers more efficient, more effective, more productive and more engaged.

For healthcare, we are in a critical moment where the industry's most pressing needs demand innovative responses and leadership from the marketplace. The clinicians, administrators and care teams at health organizations face challenges that multiply and intensify every year, making it increasingly difficult for providers to deliver consistently high quality care. Clinician burnout, declining patient satisfaction, increased financial pressures, growing administrative demands and obstacles to effective care delivery, these have profound repercussions on patient care. And the pandemic has made finding solutions to these problems even more imperative.

Beyond healthcare and across a range of industries, enterprises are consistently looking for omni-channel intelligent engagement technologies to address the current challenges around customer experience. Technologies like advanced voice-enabled solutions can help them facilitate more personal, affordable and effective connections. Our desire to address these challenges with powerful solutions was what led to the partnership with Microsoft about 1.5 years ago. Recognizing our distinctive areas of expertise are highly complementary, we brought together our AI and cloud technologies to accelerate the delivery of ambient clinical intelligence, which improves the lives of healthcare professionals and enhances the overall quality of patient care.

Over the course of our partnership, we launched our ambient clinical intelligence solution that Nuance Dragon Ambient eXperience, or DAX for short, on Microsoft Azure. And then amid the unprecedented migrations to remote care during the pandemic, we further collaborated to rapidly create an integration for Nuance DAX with Microsoft Teams to broadly scale virtual concerts.

Nuance is already a leader in conversational AI and ambient clinical intelligence, and our successful partnership with Microsoft provides us a unique opportunity to further build on our position and reach in healthcare in key enterprise verticals globally. For more than 20 years, we have built deep domain expertise across industries, including healthcare, financial services, telecommunications, retail, government and more. As Satya touched on, our industry-leading products serve large enterprises across the Fortune 100, and our healthcare solutions empower more than 550,000 physicians and 10,000 global healthcare organizations.

We are also taking the lead in redefining the paradigm of the 21st century healthcare by entering care delivery on the patient/physician experience. DAX enables the physician to focus completely on the patient by providing clinical documentation that writes itself. Nuance's solutions work seamlessly with core healthcare systems, including long-standing relationships with electronic health records or EHRs, to alleviate the burden of clinical documentation and empower providers to deliver better patient experiences.

Beyond our clinical -- clinician-focused solution, our PowerScribe One solution is a leading solution for radiology reports. We continue to expand our portfolio of radiology solutions with added intelligence to increase follow-up compliance and clinical best practices. And we foresee plenty of room to grow. Our healthcare cloud grew 37% last fiscal year, and we project continued momentum over the next couple of years. And beyond the healthcare sector, the large organizations, we see powering intelligent engagement with voice, digital and biometric solutions as a way that creates superior customer experiences, while reducing cost for the enterprise.

With the backdrop of this dynamic period of transformation for healthcare, any business organization worldwide had belief strongly that scaling and formalizing the partnership with Microsoft at this moment is the best business, strategic and economic decision. Formally joining forces will amplify our ability to deliver products that shape the future of work, help solve healthcare's most pressing challenges, and bring compelling value to our customers. And with Microsoft's cloud infrastructure, we can get our solutions to the doctors' hands even faster. Equally important, our highly differentiated AI applications will advance Microsoft's cloud strategy. And together, we will be able to address even more opportunities to significantly accelerate the application of AI and speech recognition, natural language processing and intelligent engagement across the industries.

We can reach healthcare systems globally in a way we cannot easily reach them before. At the same time, this combination offers a critical opportunity to deliver meaningful and certain value to our shareholders, who have driven and supported us on this journey.

In a world where technology innovation, the speed of change, cloud accessibility and scale are key differentiators to our customers, together, we have an extraordinary opportunity to define the future and accelerate the reach of our technology and our ambitions. In many ways, our reasons for coming together 18 months ago are the same reasons that we believe we can do even more by officially joining forces today. Our belief in the power of this combination has only gotten stronger as the changes and challenges in the critical industries we serve have continued to evolve.

With that, over to you, Scott.

Scott Guthrie {BIO 15931914 <GO>}

Thank you, Mark. As you can tell, we're incredibly excited about today's announcement. Building on the strategic alignment that Satya and Mark outlined and the impact we're already making together, I'd like to highlight a few additional areas of opportunity, both in healthcare and for every industry. Let's take a closer look at a few of these scenarios.

If you visited a doctor's office in the US recently, chances are good that your physician used Nuance solutions to document your visit. After you went home, they probably spent time speaking their notes into a solution like Nuance's Dragon

Medical One, a speech recognition solution built on Microsoft Azure and tailored for healthcare. In the future, we can bring Nuance's deep domain expertise and the relationships with core healthcare systems like EHR, electronic health records, together with Microsoft's advanced AI capabilities. By augmenting Microsoft's Cloud for Healthcare solution with Nuance's technology, healthcare providers will be able to spend more time focusing on patients, not paperwork, and continue to optimize the flow of the day-to-day work.

Beyond speech recognition, we see an opportunity to empower providers further with ambient clinical intelligence, which is exactly what we're doing with the Nuance Dragon Ambient eXperience. Mark talked about the incredible impact that DAX is having in the marketplace today, including the integration with Microsoft Teams to provide ambient clinical intelligence during telehealth visits. We're excited about this technology and proud that it's already running on Microsoft Azure.

In the future, we believe we can further scale DAX through Microsoft's global presence as well as further enhance the product through our deep AI capabilities, unlocking additional opportunities across the Microsoft Cloud for Healthcare. We envision a wide range of AI-enabled services tapping into our best-in-class Azure AI capabilities and leveraging our existing healthcare integrations like the Azure API for Fire.

When I see DAX in action, it's also clear that this technology can be applied beyond healthcare, and Microsoft can do that. We can bring this understanding of conversations to other industries that rely on that same modality. As just one example, think about conversations you could have with your financial advisor, where ambient AI could document the plan and suggest next steps to your financial advisor. Nearly any professional service could benefit from real-time engagement converted into material intelligence that drives actions. Every customer I talk to is looking to make the right decision at the right time for all of their stakeholders. Nowhere is this more true than in physician/patient engagement. We believe AI can help.

There's one critical scenario we can look at as an example: medical imaging. Medical imaging makes up a staggering portion of all healthcare data. Going back to that hypothetical doctor's visit, if you had an X-Ray taken, it's very likely the radiologists who review the image are already using Nuance to create the radiology report. In the future through our combined AI expertise, healthcare industry expertise and strong partner ecosystems, we can work with our partners in medical imaging to deliver AI and computer vision services for radiologists that reduce the time from imaging to diagnosis and diagnosis to treatment and add value throughout the imaging workflow.

Beyond healthcare, Nuance and Microsoft can take their combined AI expertise to all industries. By bringing conversational AI solutions, like interactive voice response, together with the breadth and depth of Microsoft's cloud portfolio, we believe we'll be able to deliver AI-driven digital engagement solutions for any industry scenario. Microsoft solutions like Dynamics 365 or Teams, can be augmented with new AI-

powered capabilities, adding more intelligence to any customer engagement. And Nuance's biometric security expertise can bring new capabilities to solutions like Dynamics 365 fraud protection, enabling true omnichannel end-to-end fraud protection for businesses and individuals alike.

In addition to these specific scenarios, we see structural opportunities as well. Let me touch on a few. With Microsoft's global cloud infrastructure, we will enable dramatic global scale for Nuance technology. Our partner ecosystems will be able to build differentiated solutions, leveraging both Microsoft and Nuance capabilities, whether working with leading EHR providers, like Epic and Cerner, or leading partners in other industries. Microsoft's field and distribution channels will enable us to reach new customers in new segments and geographies, broadening the reach of Nuance's technologies beyond the United States.

And this is just the beginning of what we envision together. We're excited about the opportunity to empower healthcare providers and advance our AI leadership across every industry with this acquisition.

To close this out, let me hand it over to Amy Hood.

Amy Hood {BIO 18040963 <GO>}

Thanks, Scott. Over the past seven years, we've taken a consistent approach to mergers and acquisitions of all sizes. We focus on TAM-expansive opportunities in high-growth markets, where we can uniquely add value to the users or the community. And we execute those transactions at a price that supports long-term shareholder value creation. As Satya, Mark and Scott discussed, Nuance meets those criteria. And with all acquisitions, value was ultimately only created with terrific execution, buying aligned team with a shared vision of the future. For this, key indicators of our success will be accelerated topline growth of Nuance's business and starting with Microsoft Cloud for Healthcare, increased adoption of Azure, Teams and Dynamics 365 across industries.

Now let's turn to the transaction details. We've agreed to acquire Nuance for $56 per share, implying a 23% premium to Nuance's closing price on April 9th, in an all-cash transaction valued at $19.7 billion. The acquisition will not impact our previously-announced share buyback program. The transaction has been unanimously approved by the Boards of Directors of both Microsoft and Nuance. The transaction is intended to close by the end of this calendar year, subject to approval by Nuance shareholders and the satisfaction of certain regulatory approvals and other customary closing conditions.

On a non-GAAP basis, we anticipate the transaction will be minimally dilutive or less than 1% to EPS in FY '22 and accretive in FY '23. In this context, non-GAAP excludes the expected impact of purchase accounting adjustments as well as the integration and transaction-related expenses. Following the close of the transaction, we expect to report results for Nuance in our Intelligent Cloud segment, and Mark Benjamin will remain CEO of Nuance, reporting to Scott Guthrie.

As you've heard from all of us this morning, we're well positioned to be able to further empower healthcare providers and advance cross-industry enterprise AI with differentiated, high-value solutions and a platform to support our customers and partners' future innovation. And we're confident that together, our product and go-to-market opportunities will drive long-term revenue growth.

And with that, thank you all for joining us for this exciting announcement.