

**AVANOS**

**THIRD  
QUARTER  
2018  
EARNINGS  
CALL**

**November 6, 2018**

# AGENDA AND SPEAKERS



**Joe Woody**  
*Chief Executive Officer*

Progress on 2018 Priorities  
ΔVΔNOS Outlook



**Steve Voskuil**  
*Chief Financial Officer*

Third Quarter Financial Performance  
2018 Earnings Outlook

Q&A

# OVERVIEW

## FORWARD-LOOKING INFORMATION

Certain matters in this presentation and conference call, including our 2018 outlook, expectations and planning assumptions, and any estimates, projections, and statements relating to our business plans, objectives, or the divestiture of our Surgical & Infection Prevention business, constitute forward-looking statements and are based upon management's expectations and beliefs concerning future events impacting the Company.

These statements are subject to risks and uncertainties, including currency exchange risks, cost savings and reductions, raw material, energy, and other input costs, competition, market demand, economic condition, S&IP separation execution, availability of drugs used in our Acute Pain products, other supply chain disruptions, and legislative and regulatory actions. There can be no assurance that these future events will occur as anticipated or that the Company's results will be as estimated. Forward-looking statements speak only as of the date they were made, and we undertake no obligation to publicly update them. For a more complete listing and description of other factors that could cause the Company's future results to differ materially from those expressed in any forward-looking statements, see the Company's most recent Form 10-K and Quarterly Reports on Form 10-Q.

## NON-GAAP FINANCIAL MEASURES

Management believes that non-GAAP financial measures enhance investors' understanding and analysis of the company's performance. As such, results and outlook have been adjusted to exclude certain items for relevant time periods as indicated in the non-GAAP reconciliations to the comparable GAAP financial measures included in this presentation and in today's earnings release posted on our website ([www.avanos.com/investors](http://www.avanos.com/investors)).

# DELIVERING SOLID PERFORMANCE

- Making significant progress on transformation
  - Focused on strategic investments and growth initiatives
  - Streamlining business and managing cost base
- 10% top-line growth
- Delivered adjusted diluted EPS of \$0.37
- Maintaining full-year adjusted diluted EPS of \$1.75 - \$1.90
- Momentum continues in Interventional Pain and Digestive Health
- Game Ready already contributing to performance



# DRIVING MOMENTUM OVER THE LONG-TERM

- Strong demand for minimally invasive and non-surgical outpatient procedures
- The unmet need for non-opioid pain management solutions; recently passed SUPPORT for Patients and Communities Act
- Strong markets share in Chronic Care with international growth opportunities



# INTERVENTIONAL PAIN AND CHRONIC CARE PERFORMANCE

- Interventional Pain delivered double-digit growth in NA
  - Successful direct-to-patient ad campaign
  - Expanding in coming quarter
- Chronic Care grew mid-single digit; in-line with expectations
- Expect soft Q4 Chronic Care sales
  - Timing of distributor purchases
  - Some share loss in Oral Care
  - Long-term growth expectations remain unchanged



# ACUTE PAIN PERFORMANCE

- Acute Pain sales continue to be impacted by industry-wide headwinds
  - Drug shortage lasting longer than suppliers and pre-fillers anticipated
  - Impacted revenue growth by more than 2 points; including a 1 point effect from pre-filler not allocated drugs
- Leiters transition slowly progressing
- Headwinds expected to continue into 2019
  - Seasonality in ON-Q expected to be constrained
  - Recent distributor consolidation expected to impact lower margin IV Infusion business



# AVANOS OUTLOOK

- Absent drug shortage and pre-fill headwinds, would have expected full-year organic growth of 5% to 6%
- Excluding NA Acute Pain, expected to achieve high-single digit growth
- Due to pressures, now expect full-year organic sales growth of 2% to 3%
- Acute Pain fundamentals are solid; steady growth in accounts not impacted by headwinds

# AVANOS OUTLOOK

- Committed to improving Acute Pain performance
- Implementing management changes to capitalize on business dynamics and to strengthen strategic focus
- Deepening surgeon penetration and delivering physician education
- Building sustainable strategic partnerships

# STRATEGIC INVESTMENTS

## Clinical Studies

- Investing to support January 2020 Cat 1 CPT code for genicular nerve ablation
- Hyaluronic acid comparison study enrollment completed and six-month results expected to be published Q1 2019
- Health economic study completed showing nerve ablation more cost effective than standard of care; expect publication Q1 2019

## Reimbursement, Government and Regulatory Affairs

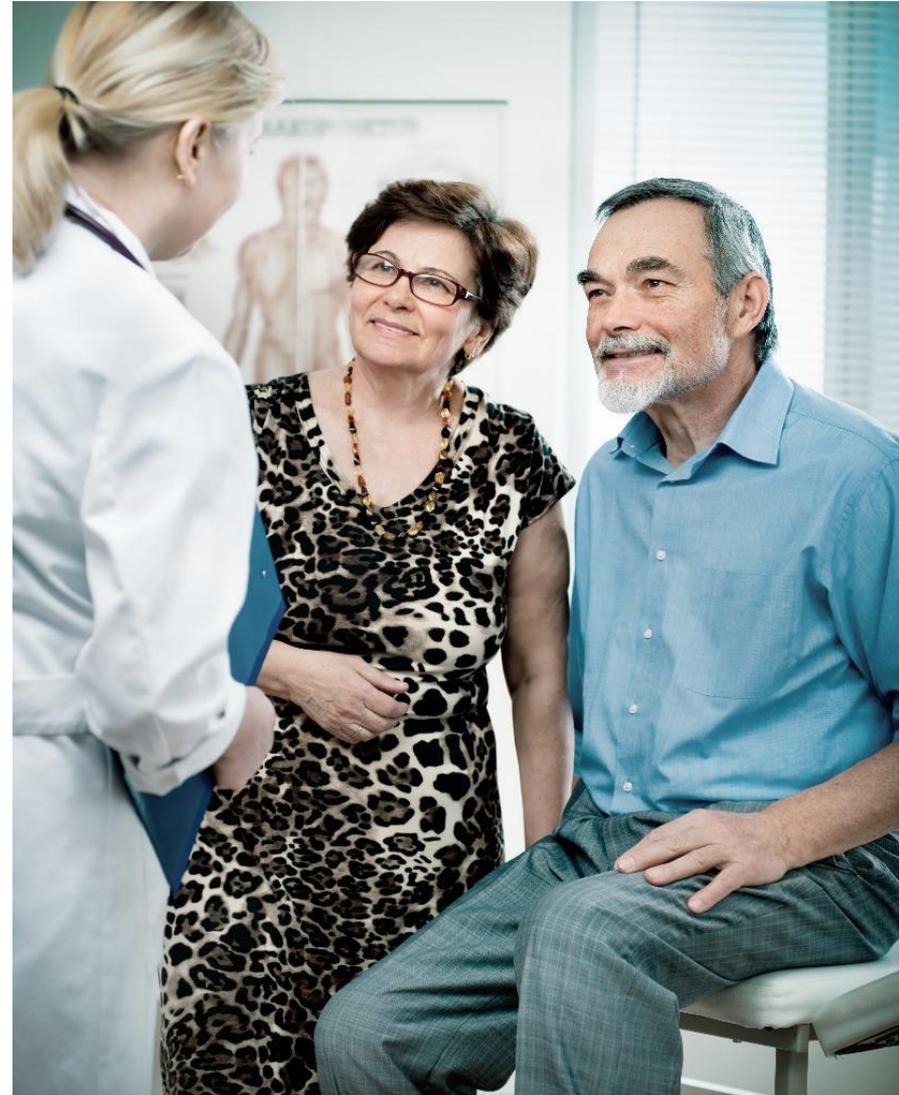
- Encouraged by opioid crisis response bill signed by the President
- Engaging with CMS to educate and encourage them to allow separate reimbursement for minimally invasive devices

## Capital Deployment

- Game Ready integration on plan and contributing to growth
- Robust M&A pipeline and actively examining opportunities

# THIRD QUARTER SUMMARY

- Confident about long-term organic growth and ability to deploy capital towards M&A
- Vigilant cost management
- Continuing transformation into a high-single digit growth company
- Focusing on delivering sustainable value



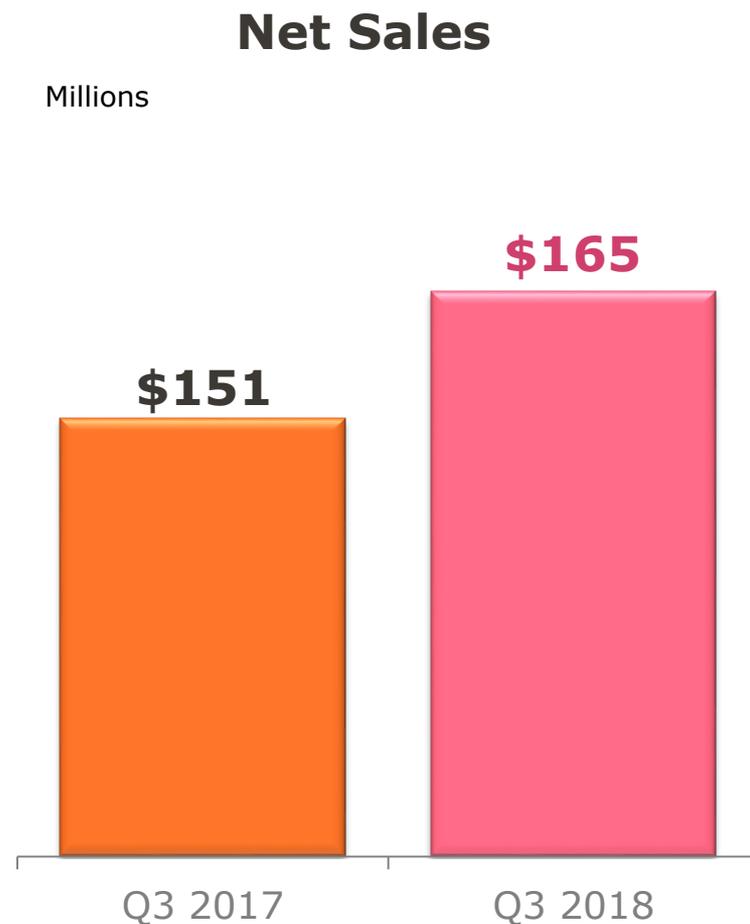
# THIRD QUARTER 2018 RESULTS

**Steve Voskuil**

Chief Financial Officer

# THIRD QUARTER PERFORMANCE

- Sales increased 10% to \$165 million, driven by:
  - Game Ready contributed 6% of growth
  - 4% volume increase, 1% unfavorable mix and lower selling prices
  - Interventional Pain, delivered double-digit growth in NA
  - Digestive Health delivered solid performance
- Expect temporary slowdown in Chronic Care in the fourth quarter
  - Timing of distributor orders
  - Loss of some Oral Care business
  - No change in view of business

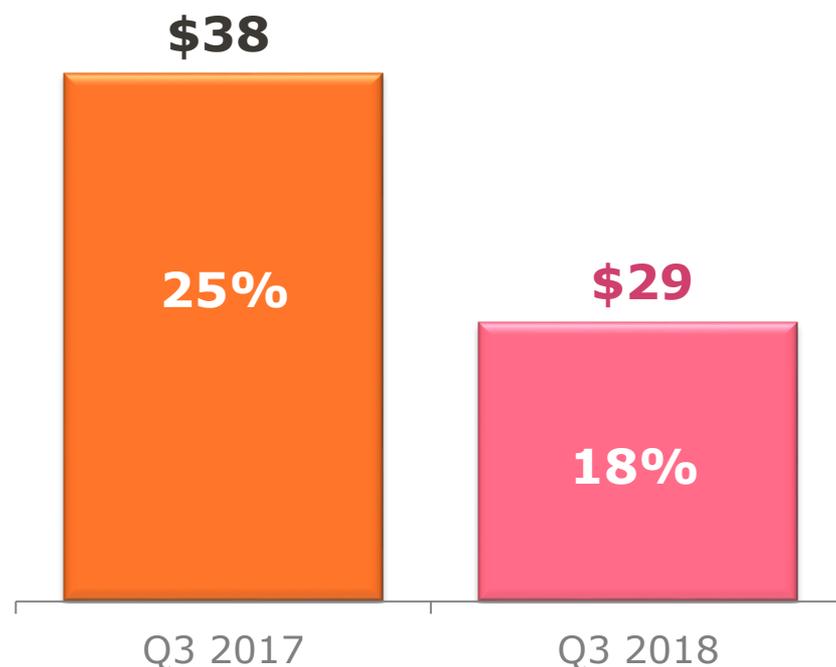


# THIRD QUARTER PERFORMANCE

- Saw continued increase in investment for short-term and long-term growth
- Accelerated funding for clinical evidence to support 2020 Cat 1 CPT code
- Elevated R&D investing
- Enhanced direct-to-patient advertising
- Increased investments and forecasted dis-synergies impacted operating profit, as expected

## Medical Device Operating Profit

Millions



# THIRD QUARTER PERFORMANCE

- Adjusted EBITDA was \$28 million, compared to \$59 million
- Adjusted net income totaled \$18 million, compared to \$28 million a year ago
- Earned adjusted diluted EPS of \$0.37
- Performance benefited from:
  - Adjusted gross margin of 65% driven by cost savings and manufacturing efficiencies; expect low 60's gross margin to return
  - Lower operating expenses despite investments in Interventional Pain and R&D projects to accelerate growth
  - Lower than expected adjusted effective tax rate

# BALANCE SHEET AND CASH FLOW

- Ended the quarter with \$412 million of cash
- Free cash flow was an \$79 million outflow
  - Largely attributable to tax payment on the gain from the S&IP divestiture
- Balance sheet remains strong
- Significant firepower to invest in growth opportunities

# 2018 OUTLOOK AND PLANNING ASSUMPTIONS

- Maintaining full-year adjusted diluted EPS of \$1.75 to \$1.90
  - Includes both continuing and discontinued operations
- Updating net sales planning assumptions due to Acute Pain business trends:
  - Regulatory headwinds lasting longer than drug suppliers and pre-fillers had anticipated
  - Consolidation of key IV Infusion distributors
  - Expect Medical Device net sales to grow 2 to 3 percent, on a constant currency basis and excluding Game Ready

# THIRD QUARTER SUMMARY

- Delivered earnings ahead of plan
- On track with post-divestiture transformation
- Strong financial profile
- Well-positioned to continue investing in growth opportunities



**Q & A**

# APPENDICIES

2018 Outlook Summary

Non-GAAP Reconciliations

# 2018 OUTLOOK SUMMARY

|   | August 7         | November 6       |
|---|------------------|------------------|
| Adjusted diluted EPS<br>Includes continuing and discontinued operations | \$1.75 to \$1.90 | \$1.75 to \$1.90 |
| Medical Device net sales, constant currency and excluding Game Ready    | 5% to 7%         | <b>2% to 3%</b>  |
| FX translation impact on net sales                                      | Even             | Even             |
| Adjusted effective tax rate   | 23% to 25%       | 23% to 25%       |
| Dis-synergies from S&IP divestiture                                     | \$15M to \$20M   | \$15M to \$20M   |

**Bold orange text indicates updated outlook**

# NON-GAAP RECONCILIATIONS

In millions

|                                 | Gross Profit                        |                |                                    |                 |
|---------------------------------|-------------------------------------|----------------|------------------------------------|-----------------|
|                                 | Three Months Ended<br>September 30, |                | Nine Months Ended<br>September 30, |                 |
|                                 | 2018                                | 2017           | 2018                               | 2017            |
| As reported                     | \$ 104.7                            | \$ 81.0        | \$ 290.5                           | \$ 247.0        |
| Restructuring and IT charges    | 1.1                                 | -              | 1.7                                | -               |
| Acquisition-related charges     | 0.4                                 | 1.2            | 0.4                                | 2.4             |
| Spin-related transition charges | -                                   | -              | -                                  | (0.3)           |
| Intangibles amortization        | 1.1                                 | 1.0            | 3.0                                | 2.9             |
| As adjusted non-GAAP            | <u>\$ 107.3</u>                     | <u>\$ 83.2</u> | <u>\$ 295.6</u>                    | <u>\$ 252.0</u> |

|   | Operating Profit (Loss)             |               |                                    |                 |
|---|-------------------------------------|---------------|------------------------------------|-----------------|
|   | Three Months Ended<br>September 30, |               | Nine Months Ended<br>September 30, |                 |
|   | 2018                                | 2017          | 2018                               | 2017            |
| As reported                                   | \$ 7.0                              | \$ (10.4)     | \$ 8.8                             | \$ (40.1)       |
| Restructuring and IT charges                  | 5.4                                 | -             | 12.2                               | -               |
| Post divestiture transition (benefit) charges | 2.3                                 | -             | (1.0)                              | -               |
| Acquisition-related charges                   | 0.8                                 | 2.0           | 1.1                                | 5.3             |
| Spin-related transition charges               | -                                   | -             | -                                  | 0.5             |
| Litigation and legal                          | 3.7                                 | 3.6           | 6.6                                | 17.3            |
| Intangibles amortization                      | 5.4                                 | 5.1           | 14.6                               | 15.5            |
| As adjusted non-GAAP                          | <u>\$ 24.6</u>                      | <u>\$ 0.3</u> | <u>\$ 42.3</u>                     | <u>\$ (1.5)</u> |

# NON-GAAP RECONCILIATIONS

In millions

|   | Income (Loss) Before Income Taxes   |           |                                    |           |
|---|-------------------------------------|-----------|------------------------------------|-----------|
|   | Three Months Ended<br>September 30, |           | Nine Months Ended<br>September 30, |           |
|   | 2018                                | 2017      | 2018                               | 2017      |
| As reported                                   | \$ 5.0                              | \$ (17.8) | \$ (8.7)                           | \$ (62.0) |
| Restructuring and IT charges                  | 5.4                                 | -         | 12.2                               | -         |
| Post divestiture transition (benefit) charges | 2.3                                 | -         | (1.0)                              | -         |
| Term Loan B retirement loss                   | -                                   | -         | 4.2                                | -         |
| Acquisition-related charges                   | 0.8                                 | 2.0       | 1.1                                | 5.3       |
| Spin-related transition charges               | -                                   | -         | -                                  | 0.5       |
| Litigation and legal                          | 3.7                                 | 3.6       | 6.6                                | 17.3      |
| Intangibles amortization                      | 5.4                                 | 5.1       | 14.6                               | 15.5      |
| As adjusted non-GAAP                          | \$ 22.6                             | \$ (7.1)  | \$ 29.0                            | \$ (23.4) |

|   | Income Tax (Provision) Benefit      |        |                                    |         |
|---|-------------------------------------|--------|------------------------------------|---------|
|   | Three Months Ended<br>September 30, |        | Nine Months Ended<br>September 30, |         |
|   | 2018                                | 2017   | 2018                               | 2017    |
| As reported                                   | \$ (0.8)                            | \$ 7.6 | \$ 2.9                             | \$ 25.5 |
| <i>Effective tax rate, as reported</i>        | <b>16.0%</b>                        | 42.7%  | <b>33.3%</b>                       | 41.1%   |
| Restructuring and IT charges                  | (1.1)                               | -      | (2.9)                              | -       |
| Post divestiture transition (benefit) charges | (0.7)                               | -      | 0.2                                | -       |
| Term Loan B retirement loss                   | 0.1                                 | -      | (1.0)                              | -       |
| Acquisition-related charges                   | (0.2)                               | (0.8)  | (0.3)                              | (2.0)   |
| Spin-related transition charges               | -                                   | -      | -                                  | (0.1)   |
| Litigation and legal                          | (0.9)                               | (1.3)  | (1.6)                              | (6.5)   |
| Intangibles amortization                      | (1.2)                               | (1.8)  | (3.5)                              | (5.8)   |
| As adjusted non-GAAP                          | \$ (4.8)                            | \$ 3.7 | \$ (6.2)                           | \$ 11.1 |
| <i>Effective tax rate, as adjusted</i>        | <b>21.2%</b>                        | 52.1%  | <b>21.4%</b>                       | 47.4%   |

# NON-GAAP RECONCILIATIONS

In millions, except per share amounts

|   | Income (Loss) from Continuing Operations |           |                   |           |
|---|--|-----------|-------------------|-----------|
|   | Three Months Ended                       |           | Nine Months Ended |           |
|   | September 30,                            |           | September 30,     |           |
|   | 2018                                     | 2017      | 2018              | 2017      |
| As reported                                   | \$ 4.2                                   | \$ (10.2) | \$ (5.8)          | \$ (36.5) |
| Diluted EPS, as reported                      | \$ 0.09                                  | \$ (0.22) | \$ (0.12)         | \$ (0.78) |
| Restructuring and IT charges                  | 4.3                                      | -         | 9.3               | -         |
| Post divestiture transition (benefit) charges | 1.6                                      | -         | (0.8)             | -         |
| Term Loan B retirement loss                   | 0.1                                      | -         | 3.2               | -         |
| Acquisition-related charges                   | 0.6                                      | 1.2       | 0.8               | 3.3       |
| Spin-related transition charges               | -  | -         | -                 | 0.4       |
| Litigation and legal                          | 2.8                                      | 2.3       | 5.0               | 10.8      |
| Intangibles amortization                      | 4.2                                      | 3.3       | 11.1              | 9.7       |
| As adjusted non-GAAP                          | \$ 17.8                                  | \$ (3.4)  | \$ 22.8           | \$ (12.3) |
| Diluted EPS, as adjusted                      | \$ 0.37                                  | \$ (0.07) | \$ 0.48           | \$ (0.26) |

|                                 | Income from Discontinued Operations, net of tax |         |                   |         |
|---------------------------------|---|---------|-------------------|---------|
|                                 | Three Months Ended                              |         | Nine Months Ended |         |
|                                 | September 30,                                   |         | September 30,     |         |
|                                 | 2018  | 2017    | 2018              | 2017    |
| As reported                     | \$ -  | \$ 26.8 | \$ 65.5           | \$ 83.0 |
| Diluted EPS, as reported        | \$ -  | \$ 0.57 | \$ 1.39           | \$ 1.78 |
| Divestiture-related charges     | -   | 5.0     | 12.9              | 5.0     |
| Gain on Divestiture             | -   | -       | (24.5)            | -       |
| Spin-related transition charges | -   | -       | -                 | (1.0)   |
| Intangibles amortization        | -   | -       | -                 | 0.4     |
| As adjusted non-GAAP            | \$ -  | \$ 31.8 | \$ 53.9           | \$ 87.4 |
| Diluted EPS, as adjusted        | \$ -  | \$ 0.68 | \$ 1.14           | \$ 1.87 |

# NON-GAAP RECONCILIATIONS

In millions, except per share amounts

|   | Net Income                          |         |                                    |         |
|---|-------------------------------------|---------|------------------------------------|---------|
|   | Three Months Ended<br>September 30, |         | Nine Months Ended<br>September 30, |         |
|   | 2018                                | 2017    | 2018                               | 2017    |
| As reported                                   | \$ 4.2                              | \$ 16.6 | \$ 59.7                            | \$ 46.5 |
| Diluted EPS, as reported                      | \$ 0.09                             | \$ 0.35 | \$ 1.27                            | \$ 1.00 |
| Restructuring and IT charges                  | 4.3                                 | -       | 9.3                                | -       |
| Post divestiture transition (benefit) charges | 1.6                                 | -       | (0.8)                              | -       |
| Divestiture-related charges                   | -                                   | 5.0     | 12.9                               | 5.0     |
| Gain on Divestiture                           | -                                   | -       | (24.5)                             | -       |
| Term Loan B retirement loss                   | 0.1                                 | -       | 3.2                                | -       |
| Acquisition-related charges                   | 0.6                                 | 1.2     | 0.8                                | 3.3     |
| Spin-related transition charges               | -                                   | -       | -                                  | (0.6)   |
| Litigation and legal                          | 2.8                                 | 2.3     | 5.0                                | 10.8    |
| Intangibles amortization                      | 4.2                                 | 3.3     | 11.1                               | 10.1    |
| As adjusted non-GAAP                          | \$ 17.8                             | \$ 28.4 | \$ 76.7                            | \$ 75.1 |
| Diluted EPS, as adjusted                      | \$ 0.37                             | \$ 0.61 | \$ 1.63                            | \$ 1.61 |

# NON-GAAP RECONCILIATIONS

In millions, except per share amounts

|   | EBITDA                              |         |                                    |          |
|---|-------------------------------------|---------|------------------------------------|----------|
|   | Three Months Ended<br>September 30, |         | Nine Months Ended<br>September 30, |          |
|   | 2018                                | 2017    | 2018                               | 2017     |
| EBITDA, as reported                           | \$ 15.9                             | \$ 44.9 | \$ 176.3                           | \$ 132.8 |
| Restructuring and IT charges                  | 5.4                                 | -       | 12.2                               | -        |
| Post divestiture transition (benefit) charges | 2.3                                 | -       | (1.0)                              | -        |
| Divestiture-related charges                   | -                                   | 8.1     | 17.4                               | 8.1      |
| Gain on Divestiture                           | -                                   | -       | (89.9)                             | -        |
| Acquisition-related charges                   | 0.8                                 | 1.9     | 1.1                                | 5.0      |
| Spin-related transition charges               | -                                   | -       | -                                  | (0.8)    |
| Litigation and legal                          | 3.7                                 | 3.6     | 6.6                                | 17.3     |
| Adjusted EBITDA                               | \$ 28.1                             | \$ 58.5 | \$ 122.7                           | \$ 162.4 |

|   | Free Cash Flow                      |         |                                    |         |
|---|-------------------------------------|---------|------------------------------------|---------|
|   | Three Months Ended<br>September 30, |         | Nine Months Ended<br>September 30, |         |
|   | 2018                                | 2017    | 2018                               | 2017    |
| Cash (used in) provided by operating activities | \$ (67.8)                           | \$ 23.4 | \$ (138.2)                         | \$ 80.1 |
| Capital expenditures                            | (10.7)                              | (14.0)  | (31.4)                             | (30.6)  |
| Free Cash Flow                                  | \$ (78.5)                           | \$ 9.4  | \$ (169.6)                         | \$ 49.5 |