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FLDM - Q3 2017 Fluidigm Corp Earnings Call

EVENT DATE/TIME: NOVEMBER 02, 2017 / 9:00PM GMT



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CORPORATE PARTICIPANTS

Ana Petrovic *Fluidigm Corporation - Director of Corporate Development and IR*

Stephen Christopher Linthwaite *Fluidigm Corporation - President, CEO & Director*

Vikram Jog *Fluidigm Corporation - CFO*

PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Fluidigm Third Quarter 2017 Financial Results Conference Call. (Operator Instructions) As a reminder, this conference is being recorded.

I would now like to turn the conference over to your host, Ms. Ana Petrovic. Please go ahead.

Ana Petrovic - *Fluidigm Corporation - Director of Corporate Development and IR*

Thank you. Good afternoon, everyone. Welcome to the Fluidigm Third Quarter 2017 Earnings Conference Call. At the close of the market today, Fluidigm released the financial results for the third quarter ended September 30, 2017.

During this call, we will review our results and provide commentary on recent commercial activity, market trends and our strategic business initiatives.

Presenting for Fluidigm today will be Chris Linthwaite, our President and Chief Executive Officer; and Vikram Jog, our Chief Financial Officer.

During the call and subsequent Q&A session, we will be making forward-looking statements about events and circumstances that have not yet occurred, including plans and projections for our business, future financial results and market trends and opportunities. Examples of these forward-looking statements include statements regarding our business prospects and growth; the implementation and anticipated benefits of strategic initiatives and partnerships; opportunities, demand, sales pipeline and support for our other product lines; benefits of new product introductions; cash management and other financial plans; and projected financial results for the fourth quarter of 2017. These statements are subject to substantial risks and uncertainties that may cause actual events or results to differ materially from current expectations. Information on these risks and uncertainties and other information affecting our business and operating results is contained in our annual report, in our most recent Form 10-Q for the quarter ended June 30, 2017, and in our other filings with the SEC.

The forward-looking statements in this call are based on the information currently available to us, and Fluidigm disclaims any obligation to update these forward-looking statements except as may be required by law.

During the call, we will also present some financial information on a non-GAAP basis. Non-GAAP information is not prepared under a comprehensive set of accounting rules and should only be used to supplement an understanding of the company's operating results as reported under U.S. GAAP. We encourage you to carefully consider our results under GAAP as well as our supplemental non-GAAP information and the reconciliation between these presentations. Reconciliations between GAAP and non-GAAP operating results are presented in a table accompanying our earnings release, which can be found in the Investors section of our website.

I will now turn the call over to Chris, our President and CEO.

Stephen Christopher Linthwaite - *Fluidigm Corporation - President, CEO & Director*

Thank you, Ana. Good afternoon, everyone, and thank you for joining our third quarter 2017 earnings call.

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The recent quarter was one in which we are fostered innovation, partnered with customers and delivered on commitments. We continued to do what we said we'd do in terms of market and customer-centric strategies, implementing cost discipline and seeking new business model efficiencies. We posted revenue within guidance. More importantly, we saw customer excitement for the evolving technology and unique value propositions we are delivering, an increased in employee engagement as Fluidigm demonstrated progress in our turn and our drive to turn the business around.

I'd like to begin by noting that on October 24, we delivered or reached a noteworthy milestone in the delivery of new breakthrough innovation to empower the global research community. Bringing Imaging Mass Cytometry to market has been a major step forward in positioning Fluidigm for a return to sustainable growth. Our Hyperion Imaging System is an expansion and broadening of our mass cytometry franchise and it joins our existing Helios suspension mass cytometry system in delivering a unique 1-2 combination of technologies in protein analysis.

In Greek mythology, Hyperion was a titan who presided over the sun. Hyperion represented light, wisdom and watchfulness. Helios, son of Hyperion, means watcher from above. Both names suggest extraordinary vision and insight and speak to our aspirations for these systems as a company. The Hyperion Imaging System is further evidence of our commitment to innovation and to answering unmet needs in high-parameter analysis, particularly in oncology, immunology and cancer immunotherapy. We envision this imaging technology becoming central to breakthrough research in these fields with significant impact on the precision medicine approaches of the future.

Hosting the launch of Imaging Mass Cytometry in Toronto last week was a great moment for Fluidigm and my most gratifying experience to date as CEO. The event included presentations from leading academic, translational and pharma research labs. It is a rare privilege, not only in life sciences, but in any industry to play a role in delivering a technological advancement as potentially significant as this platform.

We believe Hyperion could play an important role in revolutionizing disease research and bringing about the development of better diagnostics and more effective therapies. In fact, across our business, we are proud of the progress we've made in recent months and increasingly encouraged about the strategic direction we've taken.

We are innovating but we have also a steady hand on the fundamentals. We are maintaining strong discipline around internal efficiency and cost and are determined to deliver improving financial results. There is a renewed spirit and vigor at Fluidigm as we drive our strategy forward, and we're confident about the future.

I'm going to provide a brief overview of our financial results for the quarter, offer comments and context around markets and strategies and conclude with top line for 4Q or Q4 guidance. Then I'll turn the call over to our CFO, Vikram Jog, for a more detailed financial break out.

For the third quarter, total revenue was \$24.7 million, an increase of 12% from the third quarter of 2016. Instrument revenue increased 15% to \$10.5 million, primarily due to increased revenue from mass cytometry instruments, partially offset by decreased revenue from genomics instruments.

Consumables revenue increased 14% to \$10.1 million, with growth across both mass cytometry reagents and high-throughput genomics products, partially offset by decreased revenue from single-cell genomics products.

Service revenue of \$4.1 million was generally in line with the year-ago period.

Overall during the quarter, we saw more growth for mass cytometry than genomics. From a geographic standpoint, Europe and Asia posted significant growth, but we fell short of our expectations in the U.S. market.

In the U.S., competitive headwinds in single-cell and decreased revenue from genomics instruments had a disproportionate impact on our performance in comparison to other regions. In Europe, our performance reflects new commercial leadership hitting its stride, executing on funnel management with notable strong end-market demand in Germany, Eastern Europe and the U.K. Growth in Asia was driven by sales in China across both mass cytometry and genomics.

In China, we benefited from execution of our Ascendas Genomics partnership announced in quarter 2 to develop and commercialize molecular diagnostic systems and assays using BioMark HD and Juno systems.



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In Japan, I'm impressed by the strong commercial execution under the new leadership that took helm in the first half of the year. The new team is unlocking the underlying market potential in that country, particularly in mass cytometry that we knew was there. And I'm confident we'll be speaking more about this team in the coming quarters as they gain momentum.

Mass cytometry product revenue increased more than 100% to \$10.3 million from \$5.1 million in the prior year due to increased revenue from instruments and, to a lesser extent, increased revenue from consumables. We continue to focus on a targeted instrument placement strategy in key customer segments: biopharma, CROs, cancer centers and associated academic medical centers worldwide.

Let's look at how mass cytometry performed in key customer segments during the quarter. In pharma, product revenue more than doubled versus the year ago quarter, and increase 54% for the year-to-date period. In research, product revenue grew 87% versus the year ago quarter and 47% year-to-date. And in another metric that reinforces the story of a dynamic and growing business, our mass cytometry pull-through in the third quarter was well above our projected annual pull-through range for the third consecutive quarter on a larger unit base.

We continue to see strong interest from pharma customers as well as some leading translational hospital systems and compressive cancer centers as our market development activities gain traction. Let me share a few proof points.

First, in terms of key customer penetration. Mass cytometry enables the highest-parameter analysis of protein markers and genomic variance for precious blood, tissues and tumor samples of any current technology. We believe it is a must-have tool in immunology and cancer immunotherapy research. Our mass cytometry systems can be found in 22 of the 49 comprehensive cancer centers or their associated translational research institutions across the United States. This data suggests that we are in a path establishing a critical mass of installed units positioned to power future cancer research.

Second, in terms of expanding our base. Fluidigm hosted an imaging mass cytometry user group meeting in Zürich in September, attended by more than 75 early adopters and prospective buyers of the Hyperion Imaging System as well as hundreds more who viewed the event online. We saw extraordinary energy and engagement, openness and spirit of collaboration among a diverse group of academic and pharma researchers. One of the most impactful moments for me was an observation by a key external collaborator, who said they, "no longer explain how mass cytometry works, but instead focus on what insights it provides."

Third, impact stories. Our Hyperion Imaging System launch last week in Toronto featured 3 compelling presentations by leading researchers that demonstrated the power and potential of the system. We heard from Dr. Bernd Bodenmiller of the Institute of Molecular Life Sciences at the University of Zürich; Dr. Matt Silver of the Global Clinical Biomarkers and Companion Diagnostics Group at EMD Serono; and Dr. Akil Merchant of the Keck School of Medicine at the University of Southern California. I'd like to offer my personal thanks to them for participating in this important milestone event for Fluidigm.

I encourage everyone to go to the Fluidigm website and watch the event replay. It's at fluidigm.com/futureofimaging, all one word. While on our website, check out how we depict 20 parameters simultaneously in relation to one another for a tumor cell in lung tissue. It's transformative science and, frankly, I think it's very cool.

We are very excited about the enormous potential of the Hyperion system, which sets a new standard of high-multiplexed protein detection, enabling researchers to simultaneously image of 4 to 37 protein markers with minimal background and to utilize up to a total of 135 channels to detect additional parameters. The system enables identification of complex cellular phenotypes and their relationships in the context of the tissue microenvironment and is ideal for deep profiling of precious tissue samples.

We anticipate more extraordinary insights now that this technology has been launched broadly to the global research community. We believe Imaging Mass Cytometry will accelerate the pace of research already fueled by suspension mass cytometry via our Helios system.

Perhaps another key proof point is publications. The body of significantly published research based on mass cytometry continues to expand, 92 new publications year-to-date in 2017. That's added to the 318 published studies we had as of the beginning of the year. So one way to view the pace of new research is that the new studies represent a compound annual growth rate of 40%.



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Although we often speak about cancer research, many of these studies make further inroads crossing into the frontier of immunology as more diseases and conditions are linked or associated to immune system response. The insights of recent publications are profound and reflect a broadening breadth of research areas. Perhaps I'll share 3.

Stanford scientists used the mass cytometry to study how the immune system changes during pregnancy. Nearly 10% of babies are born prematurely, often with serious complications. Doctors have never had a reliable way to predict a premature birth, but it's long been suspected that the inflammatory immune response may play a role. Their hope is that they'll identify an immune signature of preterm birth, possibly one day leading to a blood test.

Second, chronic graft versus host disease, or GVHD, is a serious and too common complication of stem cell or bone marrow transplantation. Using mass cytometry, researchers at the Karolinska Institutet in Sweden, Stockholm, learned that cells of b and NKT phenotypes appear to distinguish patient groups within the disease -- or with the disease. This research may support development of a blood biomarkers that could help diagnose this disease and develop new treatments.

Third, in a study led by researchers at the University of Zurich, mass cytometry was used to survey and compare the circulating immune cells of narcolepsy patients. This study provided the most comprehensive view of the immunological signature of narcolepsy to date. This data provides a rationale for therapeutic targeting of vector T cell mechanisms to treat patients with narcolepsy.

We continue to be excited and inspired by groundbreaking research based on mass cytometry and look forward to sharing more of it with you.

Now bear in mind, these are early days, particularly for the Imaging Mass Cytometry business. While we're incredibly bullish on the long-term potential of Helios and Hyperion, we realize it will take time for the technology to gain widespread adoption across the research community.

Let's move on to high-throughput genomics. For Q3, high-throughput genomics revenue remained relatively stable for a fifth consecutive quarter. Consumables were up sequentially by 7%, in line with one of our key goals for the business.

We market our core high-throughput genomics systems in key customer segments, including biopharma, cancer centers, genome centers, clinical research labs and Ag-Bio.

And as a central strategy, we focus on reducing cost per sample while increasing flexibility and automation. A dynamic and customers-focused genomics portfolio is critical to reigniting growth for Fluidigm. Development of new content is a high priority in this business as is expansion of software solutions for interpretation and decision-making.

As you've seen in 2017, this new content is often the result of creative partnerships with customers. As examples, Fluidigm and Baylor Genetics announced in August a licensing agreement to offer a next-generation sequencing library prep assay, enabling efficient sequencing of the cystic fibrosis transmembrane conductance regulator gene. Fluidigm obtained rights to commercialize a library prep assay developed by Baylor for research use with the Juno automated microfluidic system.

A great example of innovation coming out of our pharma relationships is the Advanta Immuno-Oncology Gene Expression Assay, developed by our BioMark HD System. Advanta was announced earlier this year for that system.

We had an approximate installed base of 815 high-throughput genomics systems at the end of 2016. Across this business, we continue work on new content and seek continuing opportunities in large-scale pharma, diagnostics and other applied markets. Our primary strategic focus is to increase utilization of consumables for these systems.

High-throughput genomics is a competitive market, and we are committed to maintaining relative market share and, ultimately, to growing our share.



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Moving to single-cell. In line with expectations, we saw sequential and year-over-year revenue declines in single-cell genomics. On a year-to-date basis, single-cell product revenue represents less -- or represented less than 8% of our total product revenue. As we have noted, our single-cell assets continue to have significant value in select applications such as epigenetics, heritable changes in gene function that do not involve changes in DNA sequence. Also, as we've noted before, the Human Cell Atlas initiative is an example of an area in which our single-cell products provide a strong value proposition. However, we face significant competitive headwinds in this business with new market entrants fighting for market share.

We continue to install and support systems and innovate core technology for our customers, albeit at a different level as compared to prior years.

On our progress, strengthening each of the 3 strategic pillars. Starting with our pillar of innovation and partnership. We continue to deliver on product launch commitments, content strategy and partnership initiatives.

In addition to the agreement with Baylor I mentioned earlier, most recently, we completed a distribution agreement with the University of Zurich to offer histoCAT software for Imaging Mass Cytometry. histoCAT enables the identification of unique cellular social networks across a range of disease states. Fluidigm obtained the rights to globally distribute histoCAT in conjunction with Imaging Mass Cytometry systems.

We have undertaken a broad effort to accelerate the transition of new techniques and tools into more widespread use. Today, we are announcing the Mass Cytometry Center of Excellence initiative to develop and share suspension mass cytometry expertise. Under this initiative, researchers will work with Fluidigm to expand and refine training in mass cytometry operation and technique as well as develop new content that will be shared with Fluidigm.

Fluidigm recently completed an agreement with a major academic research entity to be the first center of excellence. Fluidigm plans to recruit additional centers in 2018 and to explore extending the initiative to Imaging Mass Cytometry.

Our strategy for innovating through customer partnerships, joint product offerings, licensing and distribution deals has been particularly successful throughout the year. Since I became CEO in late 2016, we've entered into 6 such partnerships.

Regarding our pillar of operational efficiency and cost reduction. Operating expenses for the third quarter were at the lower end of our guidance. For the first 9 months of 2017, compared to the same period a year ago, we saw a 13% reduction in our operating expenses.

Fluidigm continues to focus on value engineering, vendor negotiation and other operational expense reduction programs. We expect to achieve more than \$6 million in savings over 4 years from the exit or sublease of certain Fluidigm facilities. These savings are incremental to the approximately \$8 million in savings before severance expenses we expected in 2017 as a result of the steps taken to right-size the organization.

Fluidigm's culture is increasingly adopting this discipline of cost efficiency. I expect our business transformation office and other Fluidigm programs and initiatives to find more ways to reduce our costs and increase efficiency over time.

Finally, on our pillar of improving financial discipline and retaining talent. We've taken significant steps to manage expenses and improve our cash balance, including completion of our at-the-market or ATM equity offering, which Vikram will address in his remarks.

On the talent retention and employee engagement front, I do want to note that we have multiple programs and work streams that are informed by the feedback of our annual employee engagement survey. Recent measures have included adoption of an employee stock purchase plan and recent completion of an option exchange program.

Finally, for my remarks, fourth quarter revenue guidance. We remain optimistic regarding the remainder of the year. Specifically for the fourth quarter, we expect total revenues to be \$25.5 million to \$28.5 million.

I believe this past quarter was an affirmation that Fluidigm is a company that delivers innovation, is creative in its partnerships, is fiscally disciplined and does what it says it's going to do. Everyone at Fluidigm has been inspired and energized by the launch of the Imaging Mass Cytometry system.



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It represents the birth of an entirely new capability that we believe may unlock extraordinary biological insights, influencing and informing the future of healthcare. It speaks to our commitment to answer the unmet needs of the research community and improve the human condition.

We carry that spirit of a new, invigorated Fluidigm into the final months of 2017 and on into 2018.

I now turn the call over to Vikram, our CFO, for a further review of our financial results.

Vikram Jog - Fluidigm Corporation - CFO

Thanks, Chris, and good afternoon.

Total revenue of \$24.7 million in the third quarter increased 12% from \$22.2 million in the year ago period and was up 3% from \$23.9 million in the second quarter of 2017.

Instrument revenue of \$10.5 million in the third quarter increased 15% from \$9.2 million in the year ago period due to increased mass cytometry revenue, partially offset by lower genomics revenue.

Consumables revenue of \$10.1 million in the third quarter increased 14% from \$8.8 million in the year ago period, primarily due to increased sales from mass cytometry and high-throughput genomics products, and partially offset by lower single-cell genomics products.

In the third quarter, our annualized consumables pull-through per active system were as follows: Mass cytometry pull-through tracked above our projected range; BioMark and EP1 pull-through tracked in line with our projected range; while Access Ray, Juno and C1 pull-through tracked below our projected ranges. Consumables pull-through in the third quarter was consistent with the performance in Q2.

Services revenue of \$4.1 million in the third quarter was in line with the year ago period.

From a product perspective, genomics product revenue of \$10.3 million decreased 20% from \$12.9 million in the prior year period, mainly driven by lower single-cell genomics revenue.

Mass cytometry product revenue of \$10.3 million increased 102% from \$5.1 million in the prior year period, primarily due to increased revenue from instruments and, to a lesser extent, increased revenue from consumables.

By customer type. In the third quarter, research customers accounted for 67% of our total revenue, and applied customers accounted for the remainder.

Geographic revenues as a percentage of total revenue in the third quarter were as follows: the United States, 45%; Europe, 31%; Asia-Pacific, 20%; and other, 4%.

Year-over-year total revenues in the third quarter declined 11% in the United States and were up 48% in Europe and 34% in Asia Pacific. The decrease in the United States was mainly due to lower product revenue from single-cell genomics, impacted by a continued competitive headwinds and, to a lesser extent, lower instrument revenue from high-throughput genomics, partially offset by increased product revenue from mass cytometry.

The increase in Europe was primitive driven by higher revenue from mass cytometry and, to a lesser extent, higher revenue from high-throughput genomics products.

The increase in Asia-Pacific was due to increased revenue across both mass cytometry and high-throughput genomics.



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GAAP product margin was 44.5% in the third quarter of 2017 compared to 49.6% in the year ago period. Non-GAAP product margin was 62.1% in the third quarter of 2017 compared to 70.2% in the year ago period. Non-GAAP product margin excludes the effect of amortization of developed technology, depreciation and amortization, and stock-based compensation expense.

The year-over-year decreases in product margins were primarily due to lower production volumes of our genomics products. The decrease in GAAP product margin was partially offset by fixed amortization of developed technology over higher revenues.

Turning to OpEx. GAAP research and development expenses were \$7.7 million in the third quarter compared to \$9.3 million in the year ago period and \$7.5 million in Q2 of 2017. The year-over-year decrease is primarily due to cost reduction measures, lower stock-based compensation and lower project costs. The sequential increase is mainly due to higher project costs.

GAAP, selling, general and administrative expenses were \$20.1 million in the third quarter of 2017 compared to \$21.1 million in the year ago period and \$21 million in Q2 of 2017. The year-over-year decrease is primarily due to cost reduction measures and lower stock-based compensation. The sequential decrease is mainly due to lower legal costs and lower depreciation expense, partially offset by higher outside services.

As a result of our focus on financial discipline, for the first 9 months of 2017, operating expenses decreased by \$12.8 million or 13% on a GAAP basis and \$10 million or 11% on a non-GAAP basis compared to the year ago period.

GAAP net loss for the third quarter was \$15.9 million compared to \$19.8 million for the same period last year and \$16.9 million in Q2 of 2017. The non-GAAP net loss for the third quarter was \$8.6 million compared to \$10.9 million for the year ago period and \$9 million in Q2 of 2017.

Moving on now to the balance sheet. Accounts receivable of \$13.7 million at the end of the third quarter was flat compared to the end of Q2 2017. DSO for the third quarter was 50 days compared to 52 days in Q2 2017.

Total cash outflow in Q3, excluding net proceeds of \$28.8 million from our ATM offering, was \$8.5 million compared to \$8.2 million in Q2.

As a reminder, cash outflow in Q3 also included a \$2.8 million semiannual interest payment on our convertible debt and a net \$2 million payment under a legal settlement.

Moving on now to guidance for Q4 2017. Total revenue is projected to be between \$25.5 million and \$28.5 million. GAAP operating expenses are projected to be between \$26.5 million and \$27.5 million. Non-GAAP operating expenses are projected to be between \$23.5 million and \$24.5 million, and excludes stock-based compensation expense of approximately \$2 million and depreciation and amortization expense of approximately \$1 million. Total cash outflow is projected to be between \$2 million to \$3 million.

And with that, I will turn the call over to the operator to open it up for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And there are no questions over the phone lines at this time. I'll turn the call back over to the presenters.

Ana Petrovic - Fluidigm Corporation - Director of Corporate Development and IR

We'd like to thank everyone for attending our call. A replay of this call will be available on the Investors section of our website.

This concludes the call, and we look forward to the next update following the close of the fourth quarter of 2017.



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Good afternoon, everyone.

Operator

This concludes today's conference call. You may now disconnect.

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