ILMN Q1 2023 Earnings Call
Prepared Remarks – April 25, 2023

Salli Schwartz, ***Vice President, Investor Relations***

Hello everyone, and welcome to our earnings call for the first quarter of 2023.

During the call today, we will review the financial results released after the close of the market, and offer commentary on our commercial activity, after which we will host a question and answer session. If you have not had a chance to review the earnings release, it can be found in the Investor Relations section of our website at illumina.com.

Participating for Illumina today will be Francis deSouza, President and Chief Executive Officer, and Joydeep Goswami, Chief Financial Officer and Chief Strategy and Corporate Development Officer. Francis will provide an update on the state of Illumina's business and Joydeep will review our financial results which include GRAIL.

As a reminder, GRAIL must be held and operated separately and independently from Illumina pursuant to the interim measures ordered by the European Commission, which prohibited our acquisition of GRAIL under the EU Merger Regulation.

This call is being recorded and the audio portion will be archived in the Investor section of our website. It is our intent that all forward-looking statements regarding our financial results and commercial activity made during today's call will be protected under the Private Securities Litigation Reform Act of 1995.

Forward-looking statements are subject to risks and uncertainties. Actual events or results may differ materially from those projected or discussed. All forward-looking statements are based upon current available information, and Illumina assumes no obligation to update these statements.

To better understand the risks and uncertainties that could cause actual results to differ, we refer you to the documents that Illumina files with the Securities and Exchange Commission, including Illumina's most recent forms 10-Q and 10-K.

With that, I will now turn the call over to Francis.

Francis deSouza, ***President & Chief Executive Officer***

Thank you, Salli. Good afternoon, everyone.

Illumina delivered revenue of approximately $1.09 billion and diluted non-GAAP EPS of $0.08 in Q1, both ahead of the guidance we provided at the beginning of the year but down year-over-year, as expected. Joydeep will take you through more detail later in the call. Our focus for the rest of the year is to deliver sequential growth primarily by scaling the production and distribution of NovaSeq X, driving elasticity on the back of its increased capabilities, and improving margins. We will share more on each.

We achieved key product milestones in Q1, including shipping the first NovaSeq X systems. We also launched Illumina Complete Long Read technology and Illumina Connected Insights, a cloud-based tertiary analysis tool that addresses a key barrier to adoption, and will enable more labs to perform comprehensive genomic profiling for advanced tumors.

Turning to our performance across platforms, beginning with high-throughput.

The NovaSeq X launch further strengthened Illumina's competitive position in high-throughput sequencing. The strong global interest for the NovaSeq X series continued in Q1 and we exited the quarter with over 200 orders received from more than 30 countries.

Clinical demand continued to be stronger than expected, generating approximately 40% of orders, with some customers planning to leverage the NovaSeq X to launch new clinical offerings. About 15% of orders are from new-to-high throughput customers, like the clinical genomics lab that is leveraging NovaSeq X's ease of use and cost benefits to perform high-throughput whole genome, single cell, and RNA sequencing.

Our manufacturing capabilities for NovaSeq X instruments and consumables are scaling nicely. We shipped 67 NovaSeq X instruments in Q1, above initial expectations of 40 to 50, and now expect to deliver more than 330 NovaSeq X instruments this year – up from 300.

Customers' initial runs are showing robust data output and sequencing quality, with some customers reporting outputs greater than 7 terabases and more than 95% of bases above Q30, well ahead of published specifications.

As customers take delivery of their NovaSeq Xs and plan their deployments, they are sharing examples about how NovaSeq X will unlock demand elasticity in the sequencing market. Customers are planning to leverage the X's greater output and lower price per sample to sequence more samples, perform more analyses per sample, and obtain more data per analysis.

For example, a leading European life science research institute will use NovaSeq X to scale up its data-intensive research programs, specifically in multi-omics, spatial, and single cell, enabling them to deliver "atlas-scale" projects.

Within our clinical base, customers are using the greater output and cost savings of NovaSeq X to launch new, sequencing-intensive offerings. Some customers are planning to move from targeted panels to exomes and genomes, to achieve higher diagnostic yield and healthcare efficiency. An oncology customer is planning to use the X to launch liquid biopsy testing, which requires 12 to 15 times more sequencing than solid tumor testing.

Some customers are using the cost and turnaround time benefits to enter deeper sequencing applications like minimal residual disease, or MRD, to build datasets at scale.

We also saw continued demand for NovaSeq 6000, primarily for fleet expansions of existing workflows, and we shipped 17 NovaSeq 6000s in Q1. More than 80% of NovaSeq 6000 shipments were to clinical customers, and approximately 25% of shipments to oncology testing.

In mid-throughput, NextSeq 1k/2k unit shipments increased 6% year-over-year, as customers expand their existing fleets, or continue to shift projects from the MiSeq and NextSeq 550. More than 20% of NextSeq 1k/2k units in Q1 were placed with new-to-Illumina customers. Our win rate in the mid-throughput segment remains strong, but we are seeing some sales cycles lengthen.

Our low-throughput platforms continue to provide an entry point to sequencing. Approximately 30% of these shipments in the first quarter were to new-to-Illumina customers, further increasing our installed base and enabling adoption of sequencing across a broad customer network.

Looking now at our clinical markets…

Q1 marked an important milestone for Illumina, with clinical sequencing consumables revenue representing 50% of our total sequencing consumables revenue for the first time.

In Q1, oncology testing consumables declined 3% year-over-year but increased 21% sequentially, driven by growing clinical testing volumes and increased product development in areas like liquid biopsy and MRD. Some customers in this segment are facing pressures to improve profitability, which may in turn slow down their ability to develop new tests and scale.

Revenue from our market-leading TruSight Oncology assay, TSO 500, was greater than $25 million in the quarter, up 26% year-over-year across more than 540 accounts, driven by increased utilization and pull-through – particularly in Europe.

In March, we announced the expansion of our partnership with Myriad Genetics to broaden access to homologous recombination deficiency, or HRD, testing. HRD is an important biomarker identifying tumors with a specific type of DNA damage, like those in ovarian, breast, prostate, and pancreatic cancers. Our TSO 500 HRD, a research-use-only test, is now available in the US, with early customers like Florida Cancer Specialists & Research Institute – one of the largest independent medical oncology and hematological practices in the US. The expanded partnership also establishes a unique alliance to develop HRD as a companion diagnostic for novel agents targeting these tumors.

There was significant progress for NGS-based oncology testing reimbursement this quarter in Europe, expanding the accessible market. Seven regions in Italy committed 10 million euros for next generation sequencing in lung cancer. In Germany, health insurers commenced reimbursement for whole genome sequencing in pediatric cancer patients with relapse. And in the Czech Republic, funding for comprehensive genomic profiling was added to the national fee schedule, effective January 1st.

Also in oncology, GRAIL saw accelerating demand in Q1 for its Galleri multi-cancer early detection blood test and delivered revenue of $20 million, exceeding plan, and representing 100% growth year over year. GRAIL non-GAAP operating expenses increased to $173 million, driven primarily by investments in clinical trials and scaling GRAIL's commercial organization.

Since launch, GRAIL has received more than 85,000 Galleri test orders, with about 20,000 delivered in Q1 alone.

The 140,000-participant NHS-Galleri trial, which completed enrollment in July 2022 in just over ten months, is progressing well, with more than half of study participants having returned for their second annual blood draw. The trial recently achieved its halfway point and is currently on track to meet retention targets.

GRAIL continued to expand its partner relationships. Following a successful pilot last year, John Hancock, one of the largest life insurance companies in the US and a unit of Manulife, announced that it would expand access to Galleri to eligible life insurance customers. And Providence, a health system serving the Western US, expanded its partnership with GRAIL to offer Galleri to eligible individuals across its 52 hospitals and 900 clinics across seven states.

In reproductive health, consumables shipments declined 4% year-over-year primarily due to FX, but increased 14% sequentially due to continued coverage progress. In the US, Virginia and Michigan initiated state Medicaid coverage for NIPT in all pregnancies—adding about 4.3 million additional covered lives and more than 70,000 pregnancies per year.

Genetic Disease Testing, or GDT, had a record quarter. In Q1, GDT consumables shipments grew 7% year-over-year and 6% sequentially.

Coverage continues to grow for whole genome sequencing in patients with rare and undiagnosed genetic diseases. During the quarter, one of the largest US health insurance companies updated their policy to include Managed Medicaid lives in 16 states, adding another approximately 3.8 million covered lives for whole genome sequencing.

Also in GDT, earlier this month we announced a partnership with Henry Ford Health, a health care organization in the Detroit metro area and a leading US academic medical center, to assess how whole-genome sequencing can improve cardiovascular disease management – with a particular interest in diverse and underserved populations.

Turning to our Research and Applied markets, sequencing consumables shipments were down 19% year-over-year, primarily due to the slowdown in COVID surveillance.

Looking at the whole year, we are on track to deliver on our financial commitments for 2023 as well as some important releases in the coming quarters. Specifically, we will ship the ICLR enrichment assay – an affordable, high throughput, targeted long-read solution – in Q3 and XLEAP-SBS chemistry on NextSeq 1k/2k in the first half of 2024, delivering step-change cost, speed, and sustainability benefits on that platform.

Finally, as we navigate through this dynamic environment, we are focused on delivering durable success for our shareholders through a balance of investing in breakthrough innovations for future growth, while delivering operating leverage through disciplined expense management across the organization. To that end, we announced earlier today our commitment to deliver Core Illumina non-GAAP operating margins of 25% in 2024 and 27% in 2025, while maintaining investment in the key elements of our innovation roadmap. Building on the cost reduction actions announced last November, we are taking additional steps to reduce our annualized run rate expenses by more than $100 million beginning later in 2023. This will accelerate progress toward higher margins as well as free up capital to increase investment in high-growth areas.

I'll now turn the call over to Joydeep to discuss additional details on our results and outlook, as well as provide more detail on the steps we are taking to deliver on the cost reduction I mentioned.

Joydeep…

Joydeep Goswami, ***Chief Financial Officer, Chief Strategy and Corporate Development Officer***

Thank you, Francis.

I'll start by reviewing our consolidated financial results, followed by segment results for Core Illumina and GRAIL, and then conclude with additional remarks on our current outlook for 2023. I will be discussing non-GAAP results which include stock-based compensation. I encourage you to review the GAAP reconciliation of these non-GAAP measures which can be found in today's release and in supplementary data available on our website.

In the first quarter, consolidated revenue was $1.09 billion, up 1% from the fourth quarter of 2022, exceeding the high-end of our guidance range on stronger than expected shipments of NovaSeq X. Consolidated revenue was down 11% year-over-year, or down 9% on a constant currency basis, net of the effects of hedging. This was primarily driven by an expected year-over-year slowdown in COVID surveillance, COVID-related disruptions in China, the transition of some of our high throughput customers to NovaSeq X, and customers managing constrained capital markets globally.

Non-GAAP net income was $13 million, or $0.08 per diluted share, which included dilution from GRAIL's non-GAAP operating loss of $164 million for the quarter.

Our non-GAAP tax rate was 27.3% for the quarter, which increased from 17.8% in Q1 2022, with both quarters reflecting the impact of R&D capitalization requirements. Although the non-GAAP tax expense impact of R&D capitalization requirements in dollar terms was the same in both periods, the impact to our effective tax rate in Q1 2023 was more significant due to our lower earnings.

Our non-GAAP weighted average diluted share count for the quarter was approximately 158 million.

Moving to segment results:

Core Illumina revenue of $1.08 billion was down 12% year-over-year, which included an anticipated headwind from COVID surveillance of approximately 400 basis points. COVID surveillance contributed approximately $11 million in total revenue in Q1 2023 compared to $60 million in Q1 2022, reflecting a $49 million headwind. On a constant currency basis, Core Illumina revenue was down 10%, net of the effects of hedging.

Core Illumina sequencing consumables revenue of $692 million was up 1% sequentially, but down 12% year-over-year, which included an approximately 500 basis point headwind from COVID surveillance. In addition to the slowdown in COVID surveillance, the year-over-year decrease was primarily attributable to lower NovaSeq 6000 consumables pull-through due to the headwinds I mentioned earlier – COVID-related disruptions in China, the transition of some of our high throughput customers to NovaSeq X, and customers managing constrained capital markets globally.

Total sequencing activity on our connected high- and mid-throughput instruments grew 6% from Q4 2022 and 3% year-over-year.

Research & Applied grew 7% from Q4 2022 and declined 4% year-over-year.

Clinical sequencing activity growth remained robust, up 7% from Q4 2022 and 15% year-over-year.

As a reminder, we believe this data is a useful reference that shows the general activity trends across our installed base and is directionally correlated with revenue over time.

Sequencing instruments revenue for Core Illumina of $154 million declined 27% year-over-year, including a 300 basis point headwind from COVID surveillance. As expected, the year-over-year decrease was primarily driven by lower NovaSeq 6000 shipments compared to a record Q1 2022, and a decrease in mid-throughput shipments due primarily to fewer NextSeq 550 placements in China. Stronger than expected shipments of NovaSeq X helped partially offset this impact, although we remain supply constrained in the first year of launch. We continued to see strong demand for NextSeq 1K/2K from new-to-Illumina customers.

Core Illumina sequencing service and other revenue of $119 million was up 7% year-over-year, driven primarily by higher instrument service contract revenue on a growing installed base.

Before moving to regional results for Core Illumina, I'd like to highlight that we've implemented a new global commercial structure to improve operating efficiencies and better align with local markets. We've integrated APJ with emerging markets across Middle East, Africa, Turkey, and CIS. Going forward, we will report regional results for the following regions: Americas, Europe, Greater China and AMEA (or Asia-Pacific, Middle East, and Africa).

Americas revenue of $605 million grew 5% sequentially from Q4 2022 and exceeded our expectations due to stronger-than-anticipated shipments of NovaSeq X. Revenue for the region was down 6% year-over-year due to the expected decline in Research driven by the slowdown in COVID surveillance and delayed recruitment for some large research projects. We continued to see strong demand for NextSeq 1K/2K in the Americas, with instrument shipments up over 20% year-over-year.

Europe revenue of $261 million represented a 9% decrease year-over-year, or a 4% decrease on a constant currency basis, net of the effects of hedges. Growth in Clinical, led by oncology testing, was more than offset by the expected decline in COVID surveillance revenue as well as lower high throughput instrument shipments due to supply constraints on NovaSeq X in the first quarter.

Greater China revenue of $91 million represented a 28% decrease year-over-year, or a 23% decrease on a constant currency basis, net of the effect of hedges. The year-over-year decline was primarily driven by persistent COVID disruptions and liquidity and funding constraints at our customers. This resulted in lower sequencing consumables revenue and a decrease in mid-throughput instrument shipments compared to last year. We will continue to closely monitor and mitigate market headwinds in China through the rest of the year.

Finally, AMEA revenue of $119 million declined 27% year-over-year, or 23% on a constant currency basis, net of the effects of hedges. As expected, the year-over-year decline was primarily caused by the completion of a large research project in Japan, lower COVID surveillance revenue and a decrease in NovaSeq 6000 instrument shipments, only partially offset by NovaSeq X shipments as demand in the region outpaced supply. AMEA revenue was also impacted by sanctions affecting our ability to conduct business in Russia. We expect the impact of sanctions to persist through 2023 and have reflected approximately $60 million in lower sequencing consumables revenue expectations for the region in our outlook for 2023.

Moving to the rest of the Core Illumina P&L:

Core Illumina non-GAAP gross margin of 65.2% decreased 500 basis points year-over-year, primarily driven by less fixed cost leverage on lower manufacturing volumes, and lower instrument margins due to the NovaSeq X launch, which is typical with a new platform introduction. We expect gross margins to improve sequentially through the year as we scale NovaSeq X manufacturing and continue to drive operating efficiencies.

Core Illumina non-GAAP operating expenses of $514 million were up $9 million year-over-year primarily due to the full year impact of our headcount growth in 2022. Non-GAAP operating expenses were lower than expected as a result of cost containment initiatives.

Transitioning to the financial results for GRAIL:

GRAIL revenue of $20 million for the quarter grew 100% year-over-year driven primarily by accelerating adoption of Galleri. As expected, GRAIL revenue decreased sequentially due to a milestone payment in Q4 2022 related to MRD pharma partnerships. GRAIL non-GAAP operating expenses totaled $173 million and increased $34 million year-over-year driven primarily by continued investments in clinical trials and to scale GRAIL's commercial organization.

Moving to consolidated cash flow and balance sheet items:

- Cash flow provided by operations was $10 million;
- First quarter 2023 capital expenditures were $52 million and free cash flow was negative ($42) million;
- We did not repurchase any common stock in the quarter.

We ended the quarter with approximately $1.5 billion in cash, cash equivalents and short-term investments. During the first quarter, we used $500 million to repay the outstanding principal of our 2023 term notes that matured in March.

Moving now to 2023 guidance:

We still expect full year 2023 consolidated revenue to grow 7% – 10%, including Core Illumina revenue growth of 6% – 9%. As a reminder, these ranges include an anticipated headwind from COVID surveillance of approximately 200 basis points as well as a year-over-year headwind from foreign exchange rates. GRAIL revenue is still expected to be in the range of $90 million to $110 million for 2023.

Our revenue outlook for 2023 now reflects the following offsetting factors: (1) lower revenue in AMEA due to the impact of sanctions affecting our ability to conduct business in Russia; (2) an increase in our NovaSeq X shipment expectations to more than 330 instruments; and (3) higher contributions from our strategic partnerships related to drug discovery.

As we have previously stated, we expect quarterly Core Illumina revenue to ramp sequentially throughout 2023, with linearity trends similar to 2017 when we launched the NovaSeq 6000, where we delivered approximately 54% of our total revenue in the second half of the year, including approximately 26% in Q3 and the remainder in Q4. Our revenue ramp for 2023 reflects the following assumptions: (1) a quarterly ramp in NovaSeq X instrument shipments as manufacturing capacity improves each quarter; (2) sequencing consumables revenue increases as NovaSeq X customers kick off projects in the second half of 2023; and (3) certain macroeconomic headwinds lessen in the second half of 2023, including a recovery from COVID disruptions in China.

For fiscal 2023, at the midpoint of our revenue guidance:

- We now expect Core Illumina sequencing instrument revenue growth of approximately 13% year-over-year reflecting our higher NovaSeq X shipment expectations
- We now expect Core Illumina sequencing consumables revenue growth of approximately 5.5% year-over-year driven predominately by our lower revenue outlook for AMEA due to the impact of sanctions affecting our ability to conduct business in Russia
- We continue to expect Core Illumina sequencing revenue to grow approximately 8% year-over-year. This now includes a higher contribution from sequencing service and other revenue primarily due to higher contributions from strategic pharma partnerships.

We continue to expect non-GAAP earnings per diluted share in the range of $1.25 to $1.50 for 2023, including a consolidated non-GAAP operating margin of approximately 8% and Core Illumina non-GAAP operating margin of approximately 22%.

We are reaffirming all other financial guidance for fiscal 2023 that we provided on February 7, 2023.

Moving to the second quarter of 2023:

We expect consolidated revenue in the range of $1.150 billion to $1.170 billion for Q2 2023, reflecting a sequential increase of approximately 670 basis points from Q1 2023 at the midpoint or approximately $70 million, primarily driven by:

- A sequential increase in NovaSeq X instrument shipments as manufacturing capacity continues to ramp;
- Continued sequential growth in sequencing consumables and service revenue as new instruments continue to come online;
- A sequential increase in GRAIL revenue driven by accelerating Galleri adoption;
- Partially offset by a sequential decrease in microarrays revenue due to historical seasonality.

For the second quarter, at the midpoint of our revenue guidance range, we expect non-GAAP diluted EPS of approximately $0.01, reflecting consolidated non-GAAP operating margin of approximately 1% and Core Illumina non-GAAP operating margin of approximately 17%. These margins reflect a sequential increase in Core Illumina operating expenses driven by an increase in compensation-related expense due to our typical annual equity grant and merit adjustment in March. We continue to expect operating margins to improve in the second half of 2023 as revenue ramps and we scale our production of NovaSeq X and leverage the fixed cost of the manufacturing base.

Looking forward, we are committing to achieve Core Illumina non-GAAP operating margins of 25% in 2024 and 27% in 2025.

Illumina will reduce its annualized run rate expenses by more than $100 million beginning later in 2023. These cost savings will accelerate progress toward higher margins as well as free up capital to increase investment in high-growth areas.

Illumina will achieve these savings through a combination of several actions. We will leverage the recent modularization of R&D innovation created as part of the NovaSeq X development, including XLEAP-SBS and new flow cell technology, to lower the cost and accelerate time to market for future platforms. We will achieve additional savings through leveraging our global footprint enabling activities at more cost-effective hubs. We are also streamlining our organization and processes, including rationalization of the company's global real estate portfolio and third-party vendor spend, as well as accelerating IT optimization efforts.

The company will continue to prioritize innovations that generate highly differentiated products that are valued by Illumina's customers.

I will now invite the operator to open the line for Q&A. Thank you.

Francis deSouza, *President & Chief Executive Officer*

Thank you for joining us.

As we close the call, today is DNA Day, celebrating the 70th anniversary of the discovery of the double helix structure of DNA. This month is also Illumina's 25th anniversary. Over our history, our team has played an important role in the genomic revolution by delivering breakthrough innovations that dramatically reduce sequencing cost and broaden access to genomics, unlocking new frontiers in biology and healthcare.

And yet, today, with only 4 million genomes ever sequenced, representing only 0.07% of the population, we are still at the beginning of the genome era.

That concludes our call today.

We look forward to seeing you at upcoming conferences and other events.

Statement regarding use of non-GAAP financial measures

The company reports non-GAAP results for diluted earnings per share, net income, gross margin, operating expenses, including research and development expense, selling general and administrative expense, and from time to time, as applicable, legal contingencies and settlement, and goodwill impairment, operating income (loss), operating margin, gross profit (loss), other income (expense), tax provision, constant currency revenue growth, and free cash flow (on a consolidated and, as applicable, segment basis for our Core Illumina and GRAIL segments) in addition to, and not as a substitute for, or superior to, financial measures calculated in accordance with GAAP. The company's financial measures under GAAP include substantial charges such as amortization of acquired intangible assets among others that are listed in the itemized reconciliations between GAAP and non-GAAP financial measures included in this press release, as well as the effects of currency translation. Management has excluded the effects of these items in non-GAAP measures to assist investors in analyzing and assessing past and future operating performance, including in the non-GAAP measures related to our Core Illumina and GRAIL segments. Additionally, non-GAAP net income and diluted earnings per share are key components of the financial metrics utilized by the company's board of directors to measure, in part, management's performance and determine significant elements of management's compensation.

The company encourages investors to carefully consider its results under GAAP, as well as its supplemental non-GAAP information and the reconciliation between these presentations, to more fully understand its business. Reconciliations between GAAP and non-GAAP results are presented in the tables of this release.

The company only provides non-GAAP measures for operating margin targets because of the difficulty of projecting with reasonable certainty the financial impact of specific GAAP operating adjustments, such as acquisition-related expenses, gains and losses from our strategic investments, fair value adjustments related to contingent consideration and contingent value rights, potential future asset impairments, restructuring activities, and the ultimate outcome of pending litigation without unreasonable effort. These items are uncertain, inherently difficult to predict, depend on various factors, and could have a material impact on GAAP measures for the operating margin target periods. For the same reasons, the company is unable to address the significance of the unavailable information, which could be material to future results.

Use of forward-looking statements

This release may contain forward-looking statements that involve risks and uncertainties. Among the important factors to which our business is subject that could cause actual results to differ materially from those in any forward-looking statements are: (i) changes in the rate of growth in the markets we serve; (ii) the volume, timing and mix of customer orders among our products and services; (iii) our ability to adjust our operating expenses to align with our revenue expectations; (iv) our ability to manufacture robust instrumentation and consumables; (v) the success of products and services competitive with our own; (vi) challenges inherent in developing, manufacturing, and launching new products and services, including expanding or modifying manufacturing operations and reliance on third-party suppliers for critical components; (vii) the impact of recently launched or pre-announced products and services on existing products and services; (viii) our ability to modify our business strategies to accomplish our desired operational goals; (ix) our ability to realize the anticipated benefits from prior or future actions to streamline and improve our R&D processes, reduce our operating expenses and maximize our revenue growth; (x) our ability to further develop and commercialize our instruments, consumables, and products, including Galleri, the cancer screening test developed by GRAIL, to deploy new products, services, and applications, and to expand the markets for our technology platforms; (xi) the risks and costs associated with our ongoing inability to integrate GRAIL due to the interim measures imposed on us by the European Commission as a result of their prohibition of our acquisition of GRAIL and an order issued by the Federal Trade Commission requiring that we divest GRAIL; (xii) the risks and costs associated with the integration of GRAIL's business if we are ultimately able to integrate GRAIL; (xiii) the risk that disruptions from the consummation of our acquisition of GRAIL and associated legal or regulatory proceedings, including related appeals, or obligations will harm our business, including current plans and operations; (xiv) the risk of incurring fines associated with the consummation of our acquisition of GRAIL and the possibility that we may be required to divest all or a portion of the assets or equity interests of GRAIL on terms that could be materially worse than the terms on which we acquired GRAIL; (xv) our ability to obtain approval by third-party payors to reimburse patients for our products; (xvi) our ability to obtain regulatory clearance for our products from government agencies; (xvii) our ability to successfully partner with other companies and organizations to develop new products, expand markets, and grow our business; (xviii) uncertainty, or adverse economic and business conditions, including as a result of slowing or uncertain economic growth, COVID-19 pandemic mitigation measures, or armed conflict; (xix) the application of generally accepted accounting principles, which are highly complex and involve many subjective assumptions, estimates, and judgments and (xx) legislative, regulatory and economic developments, together with other factors detailed in our filings with the Securities and Exchange Commission, including our most recent filings on Forms 10-K and 10-Q, or in information disclosed in public conference calls, the date and time of which are released beforehand. We undertake no obligation, and do not intend, to update these forward-looking statements, to review or confirm analysts’ expectations, or to provide interim reports or updates on the progress of the current quarter.

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Illumina, Inc.
Condensed Consolidated Statements of Cash Flows
(In millions)
(unaudited)

	Three Months Ended	
	April 2, 2023	April 3, 2022
Net cash provided by operating activities	**$ 10**	$ 172
Net cash used in investing activities	**(56)**	(74)
Net cash (used in) provided by financing activities	**(473)**	21
Effect of exchange rate changes on cash and cash equivalents	**2**	—
Net (decrease) increase in cash and cash equivalents	**(517)**	119
Cash and cash equivalents, beginning of period	**2,011**	1,232
Cash and cash equivalents, end of period	**$ 1,494**	$ 1,351
Calculation of free cash flow:		
Net cash provided by operating activities	**$ 10**	$ 172
Purchases of property and equipment	**(52)**	(61)
Free cash flow **(a)**	**$ (42)**	$ 111

(a) Free cash flow, which is a non-GAAP financial measure, is calculated as net cash provided by operating activities reduced by purchases of property and equipment. Free cash flow is useful to management as it is one of the metrics used to evaluate our performance and to compare us with other companies in our industry. However, our calculation of free cash flow may not be comparable to similar measures used by other companies.

Illumina, Inc.
Results of Operations - Revenue by Segment
(Dollars in millions)
(unaudited)

	Three Months Ended		
	April 2, 2023	**April 3, 2022**	**% Change**
Consolidated revenue	**$ 1,087**	$ 1,223	(11)%
Less: Hedge gains	**2**	5	
Consolidated revenue, excluding hedge effect	**1,085**	1,218	
Less: Exchange rate effect	**(26)**	—	
Consolidated constant currency revenue **(a)**	**$ 1,111**	$ 1,218	(9)%
Core Illumina revenue	**$ 1,076**	$ 1,221	(12)%
Less: Hedge gains	**2**	5	
Core Illumina revenue, excluding hedge effect	**1,074**	1,216	
Less: Exchange rate effect	**(26)**	—	
Core Illumina constant currency revenue **(a)**	**$ 1,100**	$ 1,216	(10)%

(a) Constant currency revenue growth, which is a non-GAAP financial measure, is calculated using comparative prior period foreign exchange rates to translate current period revenue, net of the effects of hedges.

Illumina, Inc.
Results of Operations - Revenue by Region
(Dollars in millions)
(unaudited)

	Three Months Ended		
	April 2, 2023	April 3, 2022	% Change
AMR revenue - Core Illumina	$ 605	$ 646	(6)%
Less: Hedge gains	—	—	
AMR revenue - Core Illumina, excluding hedge effect	605	646	
Less: Exchange rate effect	—	—	
AMR constant currency revenue - Core Illumina **(a)**	$ 605	$ 646	(6)%
AMEA revenue - Core Illumina (b)	$ 119	$ 162	(27)%
Less: Hedge gains	1	1	
AMEA revenue - Core Illumina, excluding hedge effect **(b)**	118	161	
Less: Exchange rate effect	(6)	—	
AMEA constant currency revenue - Core Illumina **(a)(b)**	$ 124	$ 161	(23)%
China revenue - Core Illumina (c)	$ 91	$ 127	(28)%
Less: Hedge gains	—	—	
China revenue - Core Illumina, excluding hedge effect **(c)**	91	127	
Less: Exchange rate effect	(7)	—	
China constant currency revenue - Core Illumina **(a)(c)**	$ 98	$ 127	(23)%
Europe revenue - Core Illumina	$ 261	$ 286	(9)%
Less: Hedge gains	—	3	
Europe revenue - Core Illumina, excluding hedge effect	261	283	
Less: Exchange rate effect	(12)	—	
Europe constant currency revenue - Core Illumina **(a)**	$ 273	$ 283	(4)%

All amounts in tables are rounded to the nearest millions, except as otherwise noted. As a result, certain amounts may not recalculate using the rounded amounts provided.

Note: We implemented a new global commercial structure in Q1 2023 to improve operating efficiencies and better align with local markets. We integrated APJ with emerging markets across the Middle East, Africa, Turkey, and CIS. Beginning in Q1 2023 and going forward, we will report regional results for the following regions: Americas, Europe, Greater China and AMEA (or Asia-Pacific, Middle East, and Africa).

(a) Constant currency revenue growth, which is a non-GAAP financial measure, is calculated using comparative prior period foreign exchange rates to translate current period revenue, net of the effects of hedges.
(b) Region includes revenue from Russia and Turkey.
(c) Region includes revenue from China, Taiwan, and Hong Kong.

Illumina, Inc.
Results of Operations - Non-GAAP
(In millions, except per share amounts)
(unaudited)

TABLE 1: CONSOLIDATED RECONCILIATION BETWEEN GAAP AND NON-GAAP DILUTED EARNINGS PER SHARE:

	Three Months Ended	
	April 2, 2023	April 3, 2022
GAAP earnings per share - diluted	**$ 0.02**	$ 0.55
Cost of revenue **(b)**	**0.30**	0.25
R&D expense **(b)**	**0.01**	—
SG&A expense **(b)**	**0.22**	(0.08)
Other expense, net **(b)**	**0.08**	0.24
GILTI and U.S. foreign tax credits **(c)**	**(0.28)**	0.15
Incremental non-GAAP tax expense **(d)**	**(0.32)**	(0.07)
Income tax provision **(e)**	**0.05**	0.03
Non-GAAP earnings per share - diluted **(a)**	**$ 0.08**	$ 1.07

TABLE 2: CONSOLIDATED RECONCILIATION BETWEEN GAAP AND NON-GAAP NET INCOME:

	Three Months Ended	
	April 2, 2023	April 3, 2022
GAAP net income	**$ 3**	$ 86
Cost of revenue **(b)**	**48**	40
R&D expense **(b)**	**2**	—
SG&A expense **(b)**	**35**	(12)
Other expense, net **(b)**	**11**	38
GILTI and U.S. foreign tax credits **(c)**	**(44)**	24
Incremental non-GAAP tax expense **(d)**	**(50)**	(11)
Income tax provision **(e)**	**8**	4
Non-GAAP net income **(a)**	**$ 13**	$ 169

All amounts in tables are rounded to the nearest millions, except as otherwise noted. As a result, certain amounts may not recalculate using the rounded amounts provided.

(a) Non-GAAP net income and diluted earnings per share exclude the effects of the pro forma adjustments as detailed above. Non-GAAP net income and diluted earnings per share are key components of the financial metrics utilized by the company's board of directors to measure, in part, management's performance and determine significant elements of management's compensation. Management has excluded the effects of these items in these measures to assist investors in analyzing and assessing our past and future operating performance.
(b) Refer to the Itemized Reconciliations between GAAP and Non-GAAP Results of Operations for the components of these amounts.
(c) Amounts represent the impact of GRAIL pre-acquisition net operating losses on GILTI and the utilization of U.S. foreign tax credits.
(d) Incremental non-GAAP tax expense reflects the tax impact of the non-GAAP adjustments listed.
(e) Amounts represent the difference between book and tax accounting related to stock-based compensation cost.

Illumina, Inc.
Results of Operations - Non-GAAP (continued)
(Dollars in millions)
(unaudited)

TABLE 3: ITEMIZED RECONCILIATION BETWEEN GAAP AND NON-GAAP RESULTS OF OPERATIONS AS A PERCENT OF REVENUE:

	Three Months Ended April 2, 2023					
	Core Illumina		GRAIL	Eliminations	Consolidated	
GAAP gross profit (loss) (b)	$ 687	63.8 %	$ (25)	$ (7)	$ 655	60.3 %
Amortization of acquired intangible assets	14	1.4 %	34	—	48	4.4 %
Non-GAAP gross profit **(a)**	$ 701	65.2 %	$ 9	$ (7)	$ 703	64.7 %
GAAP R&D expense	$ 259	24.1 %	$ 86	$ (4)	$ 341	31.4 %
Acquisition-related expenses **(d)**	(1)	(0.1)%	—	—	(1)	(0.1)%
Restructuring **(g)**	(1)	(0.1)%	—	—	(1)	(0.1)%
Non-GAAP R&D expense	$ 257	23.9 %	$ 86	$ (4)	$ 339	31.2 %
GAAP SG&A expense	$ 286	26.6 %	$ 93	$ (1)	$ 378	34.8 %
Amortization of acquired intangible assets	—	—	(1)	—	(1)	(0.1)%
Acquisition-related expenses **(d)**	(20)	(1.8)%	(5)	—	(25)	(2.3)%
Restructuring **(g)**	(1)	(0.1)%	—	—	(1)	(0.1)%
Legal contingency and settlement **(h)**	(2)	(0.2)%	—	—	(2)	(0.2)%
Proxy contest	(6)	(0.6)%	—	—	(6)	(0.6)%
Non-GAAP SG&A expense	$ 257	23.9 %	$ 87	$ (1)	$ 343	31.5 %
GAAP operating profit (loss)	$ 142	13.2 %	$ (204)	$ (2)	$ (64)	(5.7)%
Cost of revenue	14	1.3 %	34	—	48	4.4 %
R&D costs	2	0.2 %	—	—	2	0.2 %
SG&A costs	29	2.7 %	6	—	35	3.0 %
Non-GAAP operating profit (loss) **(a)**	$ 187	17.4 %	$ (164)	$ (2)	$ 21	1.9 %
GAAP other (expense) income, net	$ (17)	(1.6)%	$ 2	$ —	$ (14)	(1.3)%
Strategic investment related loss, net **(e)**	15	1.4 %	—	—	14	1.3 %
Gain on Helix contingent value right **(f)**	(3)	(0.3)%	—	—	(3)	(0.3)%
Non-GAAP other (expense) income, net **(a)**	$ (5)	(0.5)%	$ 2	$ —	$ (3)	(0.3)%

All amounts in tables are rounded to the nearest millions, except as otherwise noted. As a result, certain amounts may not recalculate using the rounded amounts provided. Percentages of revenue are calculated based on the revenue of the respective segment.

Illumina, Inc.
Results of Operations - Non-GAAP (continued)
(Dollars in millions)
(unaudited)

TABLE 3 (CONTINUED): ITEMIZED RECONCILIATION BETWEEN GAAP AND NON-GAAP RESULTS OF OPERATIONS AS A PERCENT OF REVENUE:

	Three Months Ended April 3, 2022				
	Core Illumina		GRAIL	Eliminations	Consolidated	
GAAP gross profit (loss) (b)	$ 851	69.7 %	$ (29)	$ (7)	$ 815	66.6 %
Amortization of acquired intangible assets	6	0.5 %	34	—	40	3.3 %
Non-GAAP gross profit **(a)**	$ 857	70.2 %	$ 5	$ (7)	$ 855	69.9 %
GAAP and non-GAAP R&D expense	$ 238	19.5 %	$ 85	$ —	$ 323	26.4 %
GAAP SG&A expense	$ 251	20.6 %	$ 58	$ (1)	$ 308	25.2 %
Acquisition-related expenses **(d)**	(33)	(2.7)%	(3)	—	(36)	(2.9)%
Contingent consideration liabilities **(c)**	49	4.0 %	—	—	49	4.0 %
Amortization of acquired intangible assets	—	—	(1)	—	(1)	(0.1)%
Non-GAAP SG&A expense	$ 267	21.9 %	$ 54	$ (1)	$ 320	26.2 %
GAAP operating profit (loss)	$ 362	29.6 %	$ (172)	$ (6)	$ 184	15.0 %
Cost of revenue	6	0.5 %	34	—	40	3.3 %
SG&A costs	(16)	(1.3)%	4	—	(12)	(1.0)%
Non-GAAP operating profit (loss) **(a)**	$ 352	28.8 %	$ (134)	$ (6)	$ 212	17.3 %
GAAP other expense, net	$ (44)	(3.6)%	$ —	$ —	$ (44)	(3.6)%
Strategic investment related loss, net **(e)**	43	3.5 %	—	—	43	3.5 %
Gain on Helix contingent value right **(f)**	(5)	(0.4)%	—	—	(5)	(0.4)%
Non-GAAP other expense, net **(a)**	$ (6)	(0.5)%	$ —	$ —	$ (6)	(0.5)%

All amounts in tables are rounded to the nearest millions, except as otherwise noted. As a result, certain amounts may not recalculate using the rounded amounts provided. Percentages of revenue are calculated based on the revenue of the respective segment.

(a) Non-GAAP gross profit, included within non-GAAP operating profit (loss), is a key measure of the effectiveness and efficiency of manufacturing processes, product mix and the average selling prices of our products and services. Non-GAAP operating profit (loss) and non-GAAP other (expense) income, net exclude the effects of the pro forma adjustments as detailed above. Management has excluded the effects of these items in these measures to assist investors in analyzing and assessing past and future operating performance, including in the non-GAAP measures related to our Core Illumina and GRAIL segments.
(b) Reconciling amounts are recorded in cost of revenue.
(c) Amounts consist primarily of fair value adjustments for our contingent consideration liability related to the GRAIL acquisition.
(d) Amounts consist primarily of legal expenses related to the acquisition of GRAIL.
(e) Amounts consist primarily of mark-to-market adjustments and impairments from our strategic investments.
(f) Amounts consist of fair value adjustments related to our Helix contingent value right.

(g) Amounts consist primarily of employee severance costs related to restructuring activities.
(h) Amount consists of a loss related to a patent litigation settlement.

Illumina, Inc.
Results of Operations - Non-GAAP (continued)
(Dollars in millions)
(unaudited)

TABLE 4: CONSOLIDATED ITEMIZED RECONCILIATION BETWEEN GAAP AND NON-GAAP TAX (BENEFIT) PROVISION:

	Three Months Ended April 2, 2023	
GAAP tax benefit	**$ (81)**	**103.9 %**
Incremental non-GAAP tax expense **(b)**	**50**	
Income tax provision **(c)**	**(8)**	
GILTI and U.S. foreign tax credits **(d)**	**44**	
Non-GAAP tax provision **(a)**	**$ 5**	**27.3 %**

	Three Months Ended April 3, 2022	
GAAP tax provision	$ 54	38.3 %
Incremental non-GAAP tax expense **(b)**	11	
Income tax provision **(c)**	(4)	
GILTI and U.S. foreign tax credits **(d)**	(24)	
Non-GAAP tax provision **(a)**	$ 37	17.8 %

(a) Non-GAAP tax provision excludes the effects of the pro forma adjustments as detailed above. Management has excluded the effects of these items in this measure to assist investors in analyzing and assessing past and future operating performance.
(b) Incremental non-GAAP tax expense reflects the tax impact of the non-GAAP adjustments listed in Table 2.
(c) Amounts represent the difference between book and tax accounting related to stock-based compensation cost.
(d) Amounts represent the impact of GRAIL pre-acquisition net operating losses on GILTI and the utilization of U.S. foreign tax credits.

Illumina, Inc.
Reconciliation of Consolidated Non-GAAP Financial Guidance
(unaudited)

Our future performance and financial results are subject to risks and uncertainties, and actual results could differ materially from the guidance set forth below. Some of the factors that could affect our financial results are stated above in this press release. More information on potential factors that could affect our financial results is included from time to time in the public reports filed with the Securities and Exchange Commission, including Form 10-K for the fiscal year ended January 1, 2023 filed with the SEC on February 17, 2023. We assume no obligation to update any forward-looking statements or information.

TABLE 5: RECONCILIATION BETWEEN GAAP AND NON-GAAP DILUTED (LOSS) EARNINGS PER SHARE GUIDANCE:

	Fiscal Year 2023
Consolidated GAAP diluted loss per share (b)	**$(0.28) - $(0.03)**
Amortization of acquired intangible assets	1.23
Legal contingency and settlement **(c)**	0.02
Acquisition-related expenses **(d)**	0.16
Strategic investment related loss, net **(e)**	0.09
Gain on Helix contingent value right **(f)**	(0.02)
Restructuring **(g)**	0.01
GILTI and U.S. foreign tax credits **(h)**	0.42
Incremental non-GAAP tax expense **(i)**	(0.63)
Income tax provision **(j)**	0.05
Proxy contest	0.20
Consolidated non-GAAP diluted earnings per share **(a)(b)**	$1.25 - $1.50

	Q2 2023
Consolidated GAAP diluted earnings per share (b)	**$0.04**
Amortization of acquired intangible assets	0.31
Proxy contest	0.16
GILTI and U.S. foreign tax credits **(h)**	(0.24)
Incremental non-GAAP tax expense **(i)**	(0.26)
Consolidated non-GAAP diluted earnings per share **(a)(b)**	$0.01

(a) Non-GAAP diluted earnings per share excludes the effects of the pro forma adjustments as detailed above. Non-GAAP diluted earnings per share is a key component of the financial metrics utilized by the company's board of directors to measure, in part, management's performance and determine significant elements of management's compensation. Management has excluded the effects of these items in this measure to assist investors in analyzing and assessing our past and future operating performance.
(b) Amounts assume that the existing R&D capitalization requirements are not repealed in 2023 and, as a result, reflect an impact of approximately $75 million for fiscal year 2023.
(c) Amount consists of a loss related to a patent litigation settlement that occurred in Q1 2023.
(d) Amounts consist primarily of legal expenses incurred through Q1 2023 related to the acquisition of GRAIL.
(e) Amounts consist primarily of mark-to-market adjustments and impairments recognized in Q1 2023 on our strategic investments.
(f) Amount consists of a fair value adjustment recognized in Q1 2023 on our Helix contingent value right.

(g) Amounts consist primarily of employee severance costs related to restructuring activities incurred in Q1 2023.
(h) Amount represents the impact of GRAIL pre-acquisition net operating losses on GILTI and the utilization of U.S. foreign tax credits.
(i) Incremental non-GAAP tax expense reflects the tax impact related to the non-GAAP adjustments listed.
(j) Amount represents the difference between book and tax accounting related to stock-based compensation cost recognized in Q1 2023.

Illumina, Inc.
Reconciliation of Non-GAAP Financial Guidance
(unaudited)

Our future performance and financial results are subject to risks and uncertainties, and actual results could differ materially from the guidance set forth below. Some of the factors that could affect our financial results are stated above in this press release. More information on potential factors that could affect our financial results is included from time to time in the public reports filed with the Securities and Exchange Commission, including Form 10-K for the fiscal year ended January 1, 2023 filed with the SEC on February 17, 2023. We assume no obligation to update any forward-looking statements or information.

TABLE 6: RECONCILIATION BETWEEN GAAP AND NON-GAAP OPERATING MARGIN GUIDANCE:

	Q2 2023
Consolidated GAAP operating margin	**(5)%**
Amortization of acquired intangible assets	4
Proxy contest	2
Consolidated non-GAAP operating margin **(a)**	1%

	FY 2023
Consolidated GAAP operating margin	**3%**
Amortization of acquired intangible assets	4
Proxy contest	1
Consolidated non-GAAP operating margin **(a)**	8%

	Q2 2023
Core Illumina GAAP operating margin	**14%**
Amortization of acquired intangible assets	1
Proxy contest	2
Core Illumina non-GAAP operating margin **(a)**	17%

	FY 2023
Core Illumina GAAP operating margin	**20%**
Amortization of acquired intangible assets	1
Proxy contest	1
Core Illumina non-GAAP operating margin **(a)**	22%

(a) Non-GAAP operating margin excludes the effects of the pro forma adjustments as detailed above. Management has excluded the effects of these items in this measure to assist investors in analyzing and assessing past and future operating performance, including in the non-GAAP measure related to our Core Illumina segment.

Illumina, Inc.
Reconciliation of Non-GAAP Financial Guidance (continued)
(unaudited)

TABLE 7: RECONCILIATION BETWEEN GRAIL GAAP AND NON-GAAP OPERATING LOSS GUIDANCE:

		FY 2023
GRAIL GAAP operating loss	**$**	**(813)**
Amortization of acquired intangible assets		138
Acquisition-related expenses **(b)**		5
GRAIL non-GAAP operating loss **(a)**	$	(670)

(a) Non-GAAP operating loss excludes the effects of the pro forma adjustments as detailed above. Management has excluded the effects of these items in this measure to assist investors in analyzing and assessing past and future operating performance related to the GRAIL segment.
(b) Amounts consist primarily of legal expenses incurred through Q1 2023 related to the acquisition of GRAIL.

Illumina, Inc.
Reconciliation of Non-GAAP Financial Guidance (continued)
(unaudited)

TABLE 8: RECONCILIATION BETWEEN GAAP AND NON-GAAP TAX RATE GUIDANCE:

	Fiscal Year 2023	
	Current (b)	**If repealed (c)**
Consolidated GAAP tax rate	**118 %**	**57 %**
Non-GAAP tax adjustments **(a)**	(82)	(43)
Consolidated non-GAAP tax rate	36 %	14 %

(a) Non-GAAP tax adjustments reflect the tax impact related to the non-GAAP adjustments listed above in our "Reconciliation Between GAAP and Non-GAAP Diluted Earnings Per Share Guidance." Management has excluded the effect of these items in this measure to assist investors in analyzing and assessing past and future operating performance.
(b) Amounts assume that the existing R&D capitalization requirements are not repealed in 2023 and, as a result, reflect an impact of approximately $75 million.
(c) Amounts assume that the existing R&D capitalization requirements are repealed in 2023.