Zoetis Inc.

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SPEAKER: Ladies and gentlemen, the program is about to begin. Reminder that you can submit questions at any time via the Ask Questions tab on the webcast page. At this time, it is my pleasure to turn the program over to your host, Michael Risken. Please go ahead.

MICHAEL RUSKIN: Great. Thanks for joining us. Again, my name is Mike Ruskin. I'm on the B of A Life Science Tools Diagnostics and Animal Health team. And joining us for our next session from Zoetis is CFO Wendy Joseph. Wendy, thanks again for joining us.

WETTENY JOSEPH: Thanks for having me, Mike.

MICHAEL RUSKIN: Similar format to prior sessions. Shouldn't be any surprises. We're going to do 40 minutes of fireside chat. Feel free to hit me up with questions via Bloomberg, email, or via the portal and we'll work them in. Just to kick things off, Wetteny, our standard default opening question is, you recently reported 4Q results initially in fiscal year '24 guidance a couple of weeks ago. Can you run through some of the key talking points. What's that for you as you wrapped up '23? And what's top of mind as you go into 2024?

WETTENY JOSEPH: Yeah. Mike, we're very pleased to deliver strong results for the quarter. The fourth quarter came in at 8% operational growth. And that's really the third straight quarter of 8% or 9% operational growth. And we saw balanced growth from us. The US grew 9%, international grew about 8%. And you saw growth from price as well as volume and companion animal third straight double-digit growth rate at 10% as well.

And then last but not least, livestock returned to growth in 2023 in a big way, growing 6% in the quarter as well as 6% on the full year above the livestock global market growth rate. And so that really capped off 2023 on a strong note. And we had strong growth of 7% on the year, clearly growing faster than the industry once again.

And that's despite the starting point where we had some destocking in the first quarter, and then we saw some of the challenges in some markets like China, for example, as we went through the year. I think this really highlights our ability to grow faster than the market. And we issued guidance that also reflects that guidance on 2024 at 7% to 9% operational growth coming from multiple sources.

And certainly, contribution from our newest major franchise here with OA pain mAbs with both Librela and Solensia coming off of the recent launch in the US and continued growth outside the US in the markets where we already launched. Solensia also contributing to that growth for us.

And we see contribution coming from our derm franchise as well as Trio even in the face of competition. And Trio I'm sure we'll get into it in the session here, has continued to do really well despite direct competition in terms of the triple combination space. And we expect to grow the bottom line 9% to 11% at AMI on an operational basis.

And we're still making investments across our business. Certainly, you see it in the guidance in terms of R&D and other aspects of the business. And that 9% to 11% is despite having a non-recurring item in 2023 that contributed in terms of a royalty settlement in the first quarter to the tune of about $37 million.

So when you factor that on the guide of 2024, that 9% to 11% is a couple of points above that when you put those things in. And we're positioned to continue to return excess cash to our investors via our dividend, which we've announced an increase on as we've done as well as our share buybacks as well.
MICHAEL RUSKIN: OK. That's a great overview, great recap of the last couple of weeks. I want to touch on a couple things real quick from 2023. But I do want to spend most of the time talking about the future and not the past. But for us, one area where we still have a lot of questions and a lot of confusion is on the 4Q '23 margin dynamic.
You normally have some seasonality in margins where 4Q margins tend to be a little bit lower. It has to do with mix and timing, things like that. But this quarter was a little bit worse than we expected. So could you just walk us through the bridge of what happened 4Q on the margin line. Revenues were solid, but really, it was gross and operating that surprised a little bit.
WETTENY JOSEPH: Yeah. Look, I think the biggest impact we saw in our margins was from FX. We saw FX headwinds exiting the year. We saw FX headwinds, really, throughout the year come in. And there was an outsized effect from currencies like Argentina as well as Brazil and Turkey. But outsized FX effect given the devaluation in Argentina.
And as that goes through our cost of goods as well as existing receivables on the balance sheet as those get collected, it has a direct impact in terms of the FX losses that we see in those at an outsized compared to the relative proportion of our revenues that are coming from that market.
But I think we also saw some mixed impacts. And I think with mix, it's important to note that it's not just how much what was the percentage of companion animal versus percentage of livestock within them, we also saw a mix down in each category. So let me just explain a little bit what that means.
Within companion animal, you saw a bigger contribution from Librela than we anticipated going into the end of the year in the fourth quarter. With that bigger contribution from Librela as we've been saying all along, it's coming in at a margin rate that is below the company average.
So the more we outperform on Librela, the more pressure you saw on margins because the units that were producing for 2023 are at a level given the big capacity we've built to capitalize on demand as we look ahead. That means the unit costs are higher in 2023, and therefore they're dilutive to the overall company margins.
Now, in 2024, Librela margins, mAb margins as we launched in Librela and Solencia when we look at those products, you're going to see those be accretive to the company gross margins in 2024. And then as we exit '24 and get into '25 and beyond, those will be at the higher end of our companion animal innovative products. So that's the kind of journey we're on. So when we talk about mix there is mix within those categories that also saw some pressure in the fourth quarter.
And then livestock coming in at 6% on the year, clearly above what we were saying that we were expecting livestock to do. But within livestock, we saw more NFAs, which is at the lower end of the range in terms of margins for livestock, by the way. And so those are really, the that we saw exiting the year.
Clearly, if you look at our guidance for 2024, given where we see the mix coming in and so on-- of course, we're not forecasting FX other than what we know are the delayed effects. But if you set aside effects from an operational perspective, clearly we're giving the guidance here that through gross margins and bottom line, we're going to see expansion at two points at the ENI level above the revenue growth rate.
MICHAEL RUSKIN: OK. That's really helpful. The subcomponent mix shift is an interesting color. And talking about the 2024 guide, I mean, you mentioned the other income from 1Q 23. Is there anything else

we should keep in mind as we think about phasing through the year, whether it's op or non-op items for 2024?

WETTENY JOSEPH: Look, I think we expect roughly normalized growth across the year. Now, that's plus or minus a point. I'm not going to get that level of precision on a quarter by quarter basis. I think most everyone aware of how we started 2023, and though we have a relatively easy comp at the top line on the companion animal US business.

Now, if you look at international, international grew 10% companion animal last year in the first quarter. Livestock grew 12% in the first quarter. Clearly, outsized growth in the first quarter, so that presents a tough comp. Now, livestock is roughly a third of the overall revenue, so it's not going to move as much as companion animal does. But it's still a bit of a mix headwind if you look at the top line. So it's not all easy comps, if you will, is what I'm trying to say.

And then if you look at China, continues to be a headwind for us. Certainly, you saw China start to really decline in the second half of 2023. That continues through the first half of 2024. So those are the puts and takes. And I think livestock we expect to grow in the low single digits, so below the 6% that you saw more in line with the overall market for livestock, which is 2% to 4 percent-ish is what we would expect livestock to grow. So I think those are the pieces that you would consider.

And then as you walk through the bottom line, clearly, we're expecting to leverage our SG&A. We will be making investments behind our key franchises, certainly our paying franchises. We're launching DTC already. We have already launched DTC in the US behind Librela, for example. So those will be. But you saw real strong leverage of our SG&A as you look at the guidance that we issued.

We will see an uptick again in terms of growth for R&D slightly above the overall revenue growth rate. Not quite as hot as it was in 2023, but certainly still ahead. I think those are the pieces. I think the bottom line, the settlement in the first quarter certainly is a headwind. For us particularly, in the first quarter. But for the year, there are a couple of things that go the other way, right?

I mean, if you look at the fourth quarter, we had some unusual non-recurring items that happened in the fourth quarter, namely, the write down one asset that was within our operational figures, but then non-operational item there as well as contribution to our foundation, for example. So those things not repeating go the other way as you lap the fourth quarter of 2024.

MICHAEL RUSKIN: OK. All right. That's helpful. Now, I want to jump into the meat of the discussion. And first, I want to start with Librela. Obviously, a massive area of focus, so there's a lot to talk about here. First, you talked about your 4Q results coming in a little bit above your initial expectations. You also talked about, on the earnings call, thinking that you had maybe a third of that revenue being tied to stocking, which again, is not unusual or unexpected.

There's always going to be some smocking in the first quarter of a regional launch. So how do you think about Librela as you proceed now? You've got one quarter under your belt, positive feedback from vets, strong uptake. Even with that stocking, is it reasonable to expect at least some level of quarter of a quarter growth as you go into 2Q and then sort of into 1Q and then proceeding from there?

WETTENY JOSEPH: Yeah. Look, we're very pleased with how Librela has performed out of the gates. Our penetration levels, which is essentially the percentage of clinics that have the product surpassing our expectations to the point that we exited 2023 already launching DTC to bring more pet owner awareness to the solution here to drive them to the clinic. So all those levers are going really well for us on the product.

And posting 44 million on the fourth quarter, well above what we were expecting. But as we exited the year with that momentum, it also meant that there's relatively more of those that are stocking because that's the initial order some of those claims were placing. So we're putting somewhere in the quarter to a third of the total for the quarter. That would translate to about $12 to $15 million of stocking in that number.

So when you adjust for that as we go into the first quarter here, I don't want to get into specific guidance on a specific product or a specific quarter. But I do think when you factor 12 to 15 million of that number in Q4, something approaching or in the Neighborhood of what we did in the first quarter would still be pretty substantial growth for us in Q1 and about where I would expect this product to

MICHAEL RUSKIN: OK. And then, the way we've typically seen products ramp in animal health-- a lot of it's been your disclosures on Apoquel, Cytopoint, Trio-- is a relatively linear ramp. You don't get the ramps that you have in human health where the product spikes in year one or two and then kind of plateaus. In animal health you often see, if it's a 100 million year one, it's 200 year two, 300 year three, 400 year four. Obviously, regional launches or new geographies or product enhancements can swing that, but is there any reason to think that the Librela curve will be different than just that traditional penetration-driven model?

WETTENY JOSEPH: Yeah, I think overall, directionally, you're right in that expectation, and that's what we've seen in other products. It won't be perfectly linear. There's always some level of stocking that happens. We're still penetrating more clinics, even though we're above where we were expecting to exit 2023 and enter into 2024, so those may have some dynamics there as we start to launch some of the DTC, those maybe.

But overall, when you step back and you look at year on year on year, I think what you described is about what we would expect to see on the product. And keep in mind, we have experience with Librela, specifically, and Solensia in markets outside the US that we've seen those happen that way as well.

MICHAEL RUSKIN: And how do you think about further market penetration? I think one of the things we've talked about with Librela is, there's a lot of potential use cases, whether you're talking about really sick dogs or expanding into a little bit of that younger population. What have you seen in terms of-- I mean, it's been four or five months in the US now-- what have been the use cases by vets, and how can you drive that, sort of expand the market opportunity there?

WETTENY JOSEPH: Yeah, Mike, look. I think, as you can expect, we're still early in this, so I think we'll continue to analyze and see where the product is. But it is certainly important, as we continue the launch, to see that transition into moderate cases that if you look at the preexisting care with NSAIDs, you have a balance between the risk and benefit of using an NSAID on an animal that's moderate case and may not meet the case, right? But on a product with a profile of Librela, you would want to see that product going into those moderate cases, and that will really expand this as they will be on the product longer.

And so the duration of therapy is a key driver in terms of expanding this market, so we would look to see those start to happen in the product as we continue the ramp, which is very important on this. But you can imagine the initial use cases are going to be slanted more so to those older, more severe dogs. And then, as vets get more and more comfortable with the product, they'll start to use it on those moderate cases, given the safety and efficacy profile here and that will continue to drive that ramp on the product as we go from here.

MICHAEL RUSKIN: Maybe a natural fall on there, you're talking about the severe cases. I have to ask. We've gotten a lot of questions over the last couple of weeks in terms of the risk of adverse events or some safety issues with Librela. A lot of this is still really anecdotal, and it's tough to pin this down to any particular AE, but can you talk about the clinical data you've accumulated and the experience you've had with Librela in Europe, where it has been on the market a lot longer, in terms of the safety profile, in terms of how dogs respond to it, and how that's trending relative to your expectations?

WETTENY JOSEPH: Yeah, look. Monitoring adverse events is a normal course. Whenever you launch a product, you ask for those that are being dosed to report any events that they have, and we take those seriously. The great thing, as you mentioned, is that Librela has been in markets outside the US for about three years now, and we have 11 million doses globally since the launch three years ago. That gives us a lot of information, certainly, in terms of how the product is performing and what the safety and efficacy profile is.

And if you look at that 11 million doses that we've seen, we're not noticing any unusual events or signals that would cause us any significant concern on the product, and we continue to stand by the safety and efficacy of Librela according to the data that we're looking at now. Of course, there are different AEs, adverse events, that people are reporting. And by the way, there's not necessarily causations. It's just that an event has occurred and someone's reporting it.

And because it's a new product, there's a tendency to report more. And this is also, keep in mind, as I mentioned, in the initial launch, you're going to have the older dogs being treated. And so the older they are, the more likely they have co-morbidities that also occur. And if they haven't been as active prior to using the product, now they become more active, and you'll see things that you perhaps didn't see before. So I think that's normal course. And as I said, we're not seeing any unusual trends or signals here that we're observing in this product so far.

MICHAEL RUSKIN: You touched on two points there that I was going to pivot to. One was exactly as you said. It is older dogs that are more likely to have other health issues. How do you separate that? I mean, how do you control for that? Because if the dog is already 9, 10, 11, 12 years old when they start the therapy, that's a very late life patient, so how do you separate treatment versus unrelated impact?

WETTENY JOSEPH: Yeah, look. I don't know if control is the word I would use. I think there's awareness. There's learnings from other markets that we've launched and things that we've seen that certainly our vets within Zoetis will share with vets and KOLs and so on, and this is part of the process in terms of what we've learned from other markets. Certainly these older dogs are in pain, and you want to see the product being used to help them from that pain, and it doesn't necessarily have an effect on other things that they may already have or had that wasn't reported, et cetera.

So the way I look at it is there is some baseline, although there's not clear data on what is the baseline when you're not on a new drug in terms of how often are those things being reported. Some of them, you can imagine, is not zero. So if you look at, for example, ataxia, right? That's a neurological event that you see in reports with the new product being used.

But if you look at the 11 million doses so far, it's occurring-- or at least reported, I should say-- somewhere between one and two reports per 10,000. And if you consider that, that's considered rare in terms of the occurrences or the reporting. Again, there's no causation that we can identify based on the data, per se, but that's reported.

Now, with this population of older dogs that are in the initial launches here, you can imagine, again, we don't have data on the baseline, so I don't want to quote something that I don't have. But you can imagine, for those older dogs, the baseline is not likely to be zero. So you're having one to two per 10,000 is what the data is that we're looking at globally out of the 11 million doses so far.

MICHAEL RUSKIN: OK, that's really helpful. OK. Thanks so much. And then on the margin contribution point, I think you kind of really clarified that, at early stages, its decremental margins are given the ramp and then how that's going to inflect over the course of the year. Is there a dollar value in terms of revenues that we should be thinking about where once Librela is at 100 million or 75 million quarterly revenue, that's the break point, and above that, you really get that nice beneficial accretion from the product. Just how should we think about that as that continues to ramp in 2024?

WETTENY JOSEPH: Yeah, look. I think the margin ramp here is also more pronounced because-- and this is why we're confident in that we have the capacity that we need to take advantage of demand globally, right? The more capacity we build to prepare for that demand, the more pronounced that the difference is in the margin profile from the beginning as you go through and ramp up. So if you build more and more capacity, that means you have a bigger cost base.

And as you're producing units initially that aren't fully leveraging that cost base and that capacity, the unit costs are going to be higher. And so that's what happens is, as you launch on a product that you've built that kind of level of capacity for, it gives us the confidence that we have. I wouldn't think about it as a dollar amount, per se.

But keep in mind, mAbs take roughly 10 months from beginning to end to produce, and essentially we're producing products in 2024, or right now, that are not likely to be sold till the end of the year, towards the end of the year. And so that volume that we're producing in 2024 is such that it's absorbing enough of the cost that brings the unit cost down to the point that it is accretive to the 70% gross margins we have as a company, and so we already know that.

The question then becomes, what does it ramp into in 2025, and what rate of production are you exiting 2024 at, and is that going to get you all the way to those more innovative companion animal products? So we'll continue to model those out and produce accordingly, but the level of producing for 2024 is already getting us to that point that is accretive to the overall company margin levels.

MICHAEL RUSKIN: OK, that's really helpful. OK. I want to pivot to a couple other key product questions we have, and this is going to broadly go under the umbrella of competition, but it's also going to go on areas where you've had really strong innovation and really good product contribution in prior years. So first, let's talk about derm. Apoquel, Cytopoint, incredible blockbuster performance over the past decade between that combo really one of the few monopolies in animal health.

But now, after a decade, you're finally expected to see competition in 2024 with Elanco's [INAUDIBLE]. We don't the product profile yet, but it is widely anticipated, at least in the investor community. How would you characterize your expectations for Apo and Cyto in 2024, and how does the entry of a competitor change your mindset about that market?

WETTENY JOSEPH: Yeah, look, we've had a 10-year head start with Apoquel in the market, and about a seven-year head start with Cytopoint. The satisfaction levels from vets and pet owners is really, really high on these products. We've been expecting competition for quite some time, which has given us time to be able to position ourselves in the best ways possible, and we have multiple levers, really, to prepare for that, right?

And so if you look at Apoquel, we now have a chewable-- so now the third product. It's launched in a number of markets outside the US. We've seen a conversion from Apoquel to Apoquel Chewable, particularly if you look at the Western European markets, somewhere around 40% conversion. And it's happened sort of, what I say, naturally, given where pricing is basically a priority in those markets, as well as the US.

Now, the launch in the US is too early. We've just launched, essentially, at the same time that we launched Librela in the US, we've launched Apoquel Chewable in the US. So it will take some time to run through its course in this conversion, but that gives us one lever in terms of how we might address competition, but also meeting a need for pet owners, particularly, that have a preference to a chewable for dogs, to be able to be palatable versus putting it into a pill pack, et cetera.

So we do know pet owners prefer the chewable format versus the film-coat format, and that will naturally drive it. The question is, are there things that we'll do to accelerate that conversion even faster? And there are multiple levers there that we can pull.

But then, you also see Apoquel, more and more demand for Cytopoint, for example, given that we have the capacity and the inputs that we need, rather, since about a year and a half or two ago. And so we can fully capitalize on that demand, which is why you've seen over the last several quarters Cytopoint growth outpacing Apoquel as you see some of that transition as well.

And so I think that's another element that we have. Now, we don't have a label yet from a competitor to really respond to. What I would say is we have 10 years of data and experience for vets and pet owners. That counts for a lot in terms of the level of satisfaction that they have.

And so I think there may be, again, small little something that someone might come out with a differentiator. The question is, it a big enough differentiator to outweigh 10 years of really satisfied customers, and then all the other pieces that I just talked about? So we feel really good about how we're positioned here ahead of competition on these products, and we continue to innovate as well. Life cycle innovation and long-cycle formats, for example, for things like Cytopoint and so on are things that we're working on, and I think those things will continue to play out for us.

MICHAEL RUSKIN: OK, and I mean, you touched on differentiation. That was going to be an area I was going to push you on. Maybe I'll bundle mine, derm and Trio differentiation question together. There's a lot of debate on how differentiated products can be relative to Apoquel, Cytopint, and relative to Simparica Trio. You've already got NexGard Plus out there from Boehringer Ingelheim.

Elanco has talked about Credelio Quattro, and we generally know the active ingredients. So we more or less know what that's going to look like. So how would you characterize differentiation risk? Is there an area of weakness in some way that you sense, where maybe the safety profile isn't as good as it should be or the breadth isn't as good. And if it's not differentiated, is price-- how meaningful can price as a lever be relative to Trio, Apo, Cyto.

WETTENY JOSEPH: Yeah, look, I don't want to speculate too much on what differentiation someone might come out with. But I do think when you look at it, we're not fielding any significant requests from vets or pet owners that they wish the product performed better or differently, or covered this, or that, or the other-- which means, then, your risk, as you put it, Mike, of differentiation, in relative terms, then, must be relatively low, if you're not having current set of users that are banging on your door asking for something else from the product.

And so I think that's kind of how we characterize it. Again, caveat that we haven't seen the label yet and we don't know what we're competing against. So I think, look, whether price is-- I think there are lots of different levers that we have to play with that I just talked about a moment ago with respect to conversion to chewable and so on, and Cytopoint, and then, eventually, a long-acting version that I think will give us lots of leverage before we even start to think about or look at anything related to price. But we'll see what the competition comes out with, and we'll react accordingly.

But again, the level of satisfaction and the number of years of safety and efficacy data that users have-- vets in particular, but pet owners as well-- is going to be a pretty significant weight to balance against whatever someone comes out with, whether it's price or some nuance-level differentiation.

MICHAEL RUSKIN: OK, and then, focusing a little bit deeper on the para market, you know, NexGard Plus was the first competitor to Trio out there, and that was highly anticipated in the sense that BI talked about it for a while prior to launching it. And there was a lot of discounting, stocking by a lot of vendors in the standalone portfolio to try to retain share in that market. How have you seen that dynamic normalize as you exit in '23 and '24? Has some of that discounting faded a little bit? Are we back to a more normal operating environment, just to adjust for some of that lumpiness we've seen in the last year?

WETTENY JOSEPH: Yeah, look, Mike, I couldn't be more pleased with how Trio has performed in the face of competition. You're right, the level of promotion-- and by the way, there's always promotion in this space in terms of parasiticides. It's the biggest market out there. The most competitive market in animal health, arguably, is parasiticides. Every major player is in it. And so there are always promotions all the time, right?

But the level of promotion that we saw leading into just prior to the competitive approval was pretty significant, and it was also lasting much longer. And despite that, we just posted two straight quarters in the US where Trio grew 17%. Globally, about 20% and 21%, respectively. So clearly, doing really well, and it's just as important as the dollar growth is that we're gaining patient share in the back half of the year after the competitive launch has been out there.

So we're very pleased, again, given the satisfaction levels. We just talked about that for derm. Given the Head Start in the market that we have and the superior label that we have, very, very pleased with the performance and how we're positioned. We'll see what new competitors have. We expect more to come into this space. But again, that first-mover advantage, three to four years' worth of, I would say, safety and efficacy record and high satisfaction always counts for something fairly significant against a new entrant coming in. And our label, it's really hard to trump 100% efficacy on the first dose, so you'd say at best, someone can match that, right?

And then, you have fleas and ticks that matter. And there might be, again-- what I'll say is somewhere, a nuanced sort of differentiation that might be out there, for example, on some things. But again, we're not getting significant calls for, we wish the product would do x, y, or z. That puts us in a pretty good confidence level about our ability to compete and grow.

MICHAEL RUSKIN: OK, and just following up on that, I'm starting to get a couple of client questions. So we've got about 10 minutes. I want to make sure I squeeze these in.

First, just talking about both Simparica Trio and Apo/Cyto, is there any unusual seasonality we should expect in '24? I understand that there's always some seasonality with these products, but given the new launches, given some stocking or destocking by competitors, should we expect more or less normal

seasonality-- I mean, historic seasonality for the portfolio, for the derm portfolio in '24, or any weirdness there?

WETTENY JOSEPH: There isn't anything that is meaningful that I could point to. I think, as you said, there is some seasonality, particularly more pronounced, maybe, on the parasiticide side of things. We're about to enter into para season as you go into Q2 and Q3 and so on. And so certainly, that will be the normal levels.

And if you saw our guidance, we said, look, we expect mid to high-single digit growth. That's a fairly broad range. And so that takes into account different scenarios around what competition might be, the timing of that, the severity of promotional activity or what have you that might occur if and when there's competition in these spaces, or additional competition. So I think that range gives us that freedom, if you will, to operate in terms of what we might expect, but there isn't anything in particular that I would point to around seasonality. It may be a little bit in some markets here and there outside the US, but nothing meaningful.

MICHAEL RUSKIN: OK, and I've got a specific follow up on Librela. I think you talked about 11 million doses so far. Any sense on how many dogs or patients have been treated? I think you talked in the past about average time on treatment of around 8 months. I don't know if that number has changed. I mean, I imagine it was kind of trending higher, but that puts you in the like 1 to 1.5 million dogs treated. Is that a fair way to think through it?

WETTENY JOSEPH: I think that's maybe roughly right. You do you do have a fair amount of turnover at the older dogs that are 13, 14 years old. They're not going to be on the product very long because they have vulnerabilities and, obviously, end-of-life. But then, you have some moderate cases as well.

So I wouldn't apply-- I would just carefully apply that logic, if you will. But I don't have that specific data to give. But your logic is directionally, I would say, about right.

MICHAEL RUSKIN: Directionally accurate is the best. I hope for these days, so I'll take it. And then, I want to ask on price as a component of your algorithm, both in '23 and '24, and also longer-term. I mean, I think price has been a stronger lever for you and for the industry than it's been historically. It continues to be elevated, and that's phenomenal. But at the same time, it also means that volume is not contributing as much. So if you take both '23 and '24 numbers, and you strip out some of the new product contribution, and you strip out price, the underlying volume or the in-line growth is below historical levels.

Just anything you can talk to there? Is it anything, any specific products where you're seeing a lot of weakness? Is it just tied to the broader macro and vet visit trends, just trying to see if there's a return to that longer-term algorithm, where you do have more volume than price growth?

WETTENY JOSEPH: Yeah, look, I think if you look at performance historically, you've seen about two to three points of price. We've been running a little bit higher than that-- about 5-- the last couple of years. And we're saying we're going to come off that 5 a little bit, but maybe not all the way to the 2 to 3. And that's within a 7% to 9% growth rate.

Now, clearly, there's strong contribution from new product launches like the [INAUDIBLE] franchise and so on in, but there's not any meaningful shift in the business that we're seeing. Of course, there are some headwinds that we're factoring into our thinking here too, right? Products like-- if you look at markets like China, for example, that has had an outsized effect on volume.

So as we look at how we closed out the year, for example, you probably had about a point of volume globally taken off just by the China market alone given the volume declines that we expected to see and we saw in that market. So I do think you're seeing both price and volume contribution. Even as we get to

the upper end of our range on price, you're still seeing, if we're posting a 7 or an 8, 3 or so that it's been volume as we go through 2023. Of course, there was some noise in the first quarter given the destocking and so on, but we're very pleased with what we're seeing across the slate here.

I think when you get lots of existing products across our portfolio, both companion animal and livestock, and with livestock growing in that low-single digit, that does give us opportunity to see volume across a broader spectrum of products, if you will, there as well. And we've seen volume even in places where we've given price, like Draxxin, contribute. So I think we feel good about the elasticity that we're seeing in the business and our ability to continue to take price and still see volume growth. There are some outliers like China, like I said, that take a little bit of the-- give a haircut on the volumes that we're seeing.

MICHAEL RUSKIN: OK, that's better. And I have to ask you at least one actual P&L question. So let's talk about margins a little bit, and the long-term margin algorithm. You talked about Librela contribution margin, and at your analyst day last year in the summer, you guys had a great slide outlining the incremental margin contribution from monoclonal antibodies as that becomes a bigger part of the portfolio. Outside of that, any way to characterize the margin algorithm going forward? I mean you guys have done a tremendous job with margin expansion over the past decade. What's the next leg to the margin story for Zoetis?

WETTENY JOSEPH: Well, look, I think we're continuing to innovate, and the innovative products tend to drive unabated to drive price. And you're seeing mix continue to weigh on the companion animal side, which-- higher margins than livestock. So as that mix continues-- and within that, you mentioned mAbs are a really very important component of that. But it's not just mAbs. It's the overall growth rate of companion animal being higher. And then, price is the conversation we just had.

The good thing about Zoetis is that it's not just through higher-inflation, relatively speaking, periods that we've taken price. We have essentially, consistently taken 2 to 3 points, which the market expects. And so we continue to have that lever, which, again, contributes obviously to the margin rates and margin profile that we see ahead.

So those are pieces that go into the algorithm-- the mix, more companion animal, and within that, more mAbs weighing in at a higher margin rate, price continuing to drive. And I think those are the pieces. And then we're seeing the ability, because we've made significant investments in the past, particularly if you look at our field force investments going back to 2022, mid-2022-ish time frame, investments that we're making in various areas, we'll return to a point where you see R&D growth rate be more in line with revenue.

Last year was 14%, double the revenue growth rate. Next year, it's at the higher end, maybe a touch above the high end of our revenue growth rate. You'll see that normalize to be more in line with revenue, but leveraging G&A certainly is an element that you're seeing play out here. That will contribute to-- and you're seeing it play out also in that 2024 guide. Despite the royalty settlement that we've talked about, we're talking about 2 points above the revenue growth rate despite having that headwind. If you adjust for that, you've got another couple of points. So you've seen that leverage come through already as we go through 2024. I won't give more specifics beyond '24, but the algorithm or the pieces that I've just covered.

MICHAEL RUSKIN: Yeah, yeah, I mean between revenue, between what you said-- R&D investments being in a relatively elevated pace last year, this year, and the incremental contribution from Librela, sounds like there's a lot of opportunity for further margin gains going forward.

WETTENY JOSEPH: Yeah.
MICHAEL RUSKIN: [INAUDIBLE]. OK, I got a couple of minutes left. I have one-- a few more coming in from clients. One was a question on-- you touched on China a couple of times. Anything you can say more broadly in terms of current OUS trends in general, both companion and livestock? It's just a lot harder to get visibility into that, and especially because you've got your OUS reporting segment is a lot different. So you've got a much further visibility on that. Anything that's worth calling out there?
WETTENY JOSEPH: Look, I think we look outside the US. And the US is such a big market, right? But we're very diverse as a company. We're in a lot of different markets. Once you get out of the US, each individual market is somewhere, and the biggest ones are about 4% of our total revenue. So you start to see a lot of different dynamics.
But there are some consistent trends. We're continuing to see really good, strong growth, particularly across companion animal. But if you look at the emerging markets, livestock tends to drive the growth rate for livestock disproportionately out of those emerging markets, and those trends continue. I do think there are some pieces that we've talked about. So when you go through the algorithm of growth for us in 2024, you have the contribution from price. You have contribution from the pain meds. You have derm and Trio contributing, livestock contributing.
I do think there are some offsets that go into our thinking and our logic, China being one of them, given the strong comps and also the overall economic cycle we're going through in China right now. That hasn't changed. We've been talking about that for the last couple of quarters, and it remains at the levels that we expected. So I think you're going to see some headwinds in terms of the next couple of quarters because the comps are higher, in addition to the economic cycle.
We'll see how it plays out for the back half of the year. And so we're watching other markets that get impacted by China to see how those play out. We've factored some of those into our thinking in terms of our guidance already in that 7 to 9 range. But overall, I would say the strength that we're seeing in companion animal, these trends-- I've been amazed by almost three years in the company that you go to these emerging markets, and you're seeing the same demand pull coming from companion animal, to the point that companion animal now outside the US is also more than 50%. Now, it's 75% or 80% in the US, but it's more than 50% outside the US, where, even in my lifetime here, it was slightly less than 50%. So you're seeing that continue to climb as well. So that's very encouraging.
MICHAEL RUSKIN: OK, all right. Well, we'll have to end it there, unfortunately. A couple more things we could discuss, but we'll have to follow up offline. Wetteny, thanks so much for joining. I also know it's your birthday, being a leap year. So happy birthday. I don't if you're 11 or 12 this week, but it's a big day. Thanks for spending it with us. I hope you have a good set of meetings and get to enjoy some cake later this afternoon.
WETTENY JOSEPH: Thanks, Mike, really appreciate that. I get one birthday every 1460 days. The only thing that would be better is if I only aged that slowly, but I don't. [LAUGHS]
MICHAEL RUSKIN: Yeah, don't we all.
WETTENY JOSEPH: All right.
MICHAEL RUSKIN: Thanks, everyone, for joining. Thanks for letting me.
WETTENY JOSEPH: All right.
[CLASSICAL PIANO MUSIC]