Firmenich Half Year 2022 Results Presentation

Presentation

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Head of Investor Relations

Good morning and welcome to the Firmenich half year 2022 earnings call for the six months ended 31 December 2021. We are joined today by Firmenich's CEO, Gilbert Ghostine and CFO, Benoit Fouilland.

Before we begin, I would like to inform you that during this call, management will make forward-looking statements that reflect Firmenich's judgement and analysis only as of today. These forward-looking statements are not guarantees or predictions of future performance and involve known and unknown risks, uncertainties and other factors, many of which are beyond our control, and which may cause actual results to differ materially from the statements in this presentation. Listeners are cautioned not to rely on forward-looking statements.

Information disclosed on this call may be subject to updating, revision, verification and amendment and such information may change materially. We do not assume any obligation to update information, including any forward-looking statements, discussed on the call today.

Our results are reported under IFRS and today's presentation also includes reference to certain non-IFRS measures. These measures are used internally by management to assess the performance of our business, make decisions on the allocation of our resources, and assess operational management. We draw your attention to the alternative performance measurements pages in the appendix of today's presentation.

Finally, unless otherwise stated, growth comparisons made during this call are all against the same period in the prior year. Unless otherwise stated, revenue growth comparisons are made at constant currency, as defined in the alternative performance measurements pages. Now it is my pleasure to hand it over to our CEO, Gilbert Ghostine.

Gilbert Ghostine

Chief Executive Officer

Thank you, Diego. Good morning, everyone. I hope that you and your families are healthy and safe. I would like to thank you for joining us today. It is a pleasure to present to you the results for the first six months of our fiscal year 2022.

In today's presentation we will cover the following topics. First, I will review the key achievements and challenges of the past six months. Benoit will then provide an overview of our financial performance and finally, we will open up the lines for questions.

Let me turn first to the review of the last six months. In the first half of our fiscal year, we delivered a solid set of results on both top and bottom line, despite a challenging raw material and supply chain external environment.

Our revenue grew by 12%, with double-digit growth in most of our key markets and segments and we increased our adjusted EBITDA by 25%. We generated CHF162 million of free cash flow. This was 11% lower than last year, due to the impact of higher safety inventories, as we prioritised security of supply and quality of service for our customers in a challenging global context.

We are delivering against the ambitions for the fiscal year 2022 that I highlighted to you on our last call. We are accelerating our profitable organic growth, driven by continued breakthrough innovation and our strength in natural and renewable products. We are gaining share with our customers, by prioritising their security of supply in a challenging global environment and at the same time, we continue to lead the industry in ESG.

Let me now take you through the highlights of the first six months of the year. As I mentioned, we have delivered solid revenue and profitability growth across our business.

In Taste & Beyond, we continued the strong momentum seen since last year, growing revenue ahead of the industry by over 13%. This is the result of our focused innovation and share gains with strategic partner customers.

In Perfumery & Ingredients, we also delivered industry-leading revenue growth of 38% in Fine Fragrance, which has now surpassed pre-pandemic levels. Thanks to our customer intimacy and commitment to best-in-class service, we have captured the renewed consumption in this affordable luxury category, to which consumers are increasingly turning.

Our Ingredients business continues its double-digit growth, up 24%, thanks to strong customer demand supported by our vertical integration and our strength in natural and renewable ingredients. In Consumer Fragrances, we closed the first six months almost flat, mainly due to the combination of a high comparable period last year and end-market softness.

As a leading player with global reach, we are positioned to capitalise on structural growth trends in both developed and emerging markets. This first half, we grew across all our regions and delivered double-digit growth in the key geographies of Europe, India, and China and 7% growth in North America.

We are committed to deliver profitable growth and we have increased our adjusted EBITDA by over 25%, which translates to an additional 2.1 percentage points of adjusted EBITDA margin.

Firmenich has a track record of innovation driven growth, underpinned by world-class science. We focus our innovation to address the structural trends that drive industry expansion.

In the first half, we have delivered strong double-digit and even triple-digit growth in many of our key innovation initiatives, including sugar reduction, plant-based proteins, renewable fragrances and our e-commerce channel.

Let me give you a few examples of our innovative launches of the past six months. As part of our program to develop sustainable new ingredients, we launched Mugissimo. This is a new biodegradable lily-of-the-valley ingredient, developed through green chemistry, that brings elegant and fresh natural floral notes to fragrances, highly appreciated by perfumers.

Since our acquisition of Campus, we have accelerated our innovation in plant-based protein solutions. We have just launched our latest portfolio of SmartProteins innovations for the rapidly growing plant-based dairy space. Our solutions improve the creaminess and the mouthfeel of dairy, dietary and nutrition products. They allow sugar reduction and manage the off-notes from plant proteins, using familiar ingredients that are desirable to consumers.

Leveraging our leading digital capabilities to support our creators, last year we announced Scentmate, our artificial intelligence enabled fragrance co-creation platform for entrepreneurs and independent brands. We are now rolling out this platform into the growing new category of aromachology, which is at the crossroads of fragrance, human emotions and consumer behaviour.

To help consumers achieve better nutrition and wellbeing with less sugar, we have continued to develop our NutriGem nutrition innovation program, with ready-to-use integrated solutions using fibres, vitamins, minerals and natural extracts.

Consumer demand for natural, sustainable and renewable products is a structural growth trend in our industry. Our leadership in natural ingredients, our strong vertical integration and our innovation in this space are key points of differentiation for our customers.

In December, we launched Muguet Firgood, a 100% natural ingredient that combines our proprietary gentle extraction technology with the vertical farming capabilities of our French partner start-up, Jungle. This innovative ingredient is a unique addition to our palette and reinforces our leadership in naturals.

Renewability and biodegradability are increasingly important in fragrance encapsulation. This first half, we launched our first generation of biodegradable renewable capsules, and we will continue to lead the industry towards the objective of microplastic-free fragrance encapsulation.

In December, we also commissioned a new production unit for renewable ingredients in France, which will expand the production capacity of our Castets facility by 50%. This reinforces our ability to develop and produce the new renewable ingredients that our customers demand.

We take pride in being a trusted partner to our customers. The world economy is facing a challenging raw material and supply chain environment. Our industry is no exception, with inflationary pressures, raw material shortages, logistics issues and COVID-related absenteeism affecting production.

We have chosen to prioritise security of supply and quality of service for our customers, to fulfil their growing demand despite these challenges. To do this, we have increased our safety inventories above our normal levels, while leveraging our vertical integration and diversifying our sources of supply.

Although this has had an impact on our free cash flow this half year, we are confident it is the right choice in this environment, and we remain committed to preserving cash flow generation.

We are proud to be the leader in ESG in our industry. Responsible business is a core part of our values and a source of trust and differentiation for our customers, our investors and our shareholders. This first half we have continued to lead the industry in ESG.

In December, we received a refreshed rating from Sustainalytics, with a score of 7.5, further improving on our already industry-leading score of last year. This not only places us as ESG leaders in our industry and the broader chemicals sector, but also in the global top 50 of over 15,000 companies in the world.

Firmenich is one of only two companies in the world to have received a triple-A rating from CDP, in climate, water and forests, for the fourth year in a row. This is a testament to our efforts to address environmental issues through our operations.

We also achieved a second consecutive platinum sustainability rating from EcoVadis, with an industry-leading score of 88 out of 100, which places us in the top 1% of all companies assessed worldwide.

Let me now turn to our priorities for the second half of our fiscal year. Looking ahead, I would like to highlight three priorities. Firstly, we will continue to drive profitable organic growth and market share gains. We will keep focusing on high growth segments and markets, leveraging our insights to help our customers address changing consumer preferences.

We will continue delivering breakthrough innovation, reinforcing our renewable portfolio with new proprietary fragrance and taste ingredients, as well as differentiated food solutions and we will keep leveraging our digital capabilities to accelerate our transformation.

Excellence in execution is core to our success, and we will focus on balancing leading customer service with our steadfast commitment to cash generation.

Now, I would like to hand it over to Benoit for the financial review of the past six months. Benoit, over to you.

Benoit Fouilland

Chief Financial Officer

Thank you, Gilbert, and good morning, everyone. It's a pleasure to give you an update on our performance, six months into our fiscal year 2022. Firmenich delivered strong topline growth in this first half, achieving double-digit revenue growth, despite a challenging raw material and supply chain environment.

Revenue grew by 12.3% year-over-year, driven by volume growth across Perfumery & Ingredients and Taste & Beyond. In a context of improving market conditions, we achieved new business wins, thanks to our customer intimacy and service and our focused investment in growth markets and segments. In addition, we benefited from favourable product mix, mainly driven by growth in fine fragrance.

Foreign exchange had a negligible impact on revenue in this first half of the year. On a reported basis, revenue increased by 12.2% year-over-year, reaching CHF2.241 billion.

Across our global footprint, we have seen a return to growth in all regions. In Europe, we grew revenue by 22.2%, driven by performance in Fine Fragrance and Ingredients. In India, we grew by 12.9% and we generated 12.9% growth across the broader region of India, Middle East and Africa.

In China, we achieved 10.4% growth and in the entire North and East Asia region we delivered 9.5% growth. In North America, we delivered 7% growth, while Southeast Asia grew by 6% and Latin America by 3%.

As a leading player with global reach, we continually invest in our business in high growth 231 markets. In September, we opened an end-to-end fragrance and taste co-creation centre in Guangzhou, to serve customers in South China, one of the most dynamic areas of growth in this key market. This centre brings under one roof our commercial, marketing and creative teams, where they can create innovative offerings together with our customers.

In November, we began construction of a state-of-the-art production hub in Turkey. This new plant will provide 20,000 metric tons of additional capacity to serve fragrance customers in Turkey, the Middle East and the Stans countries. In line with our 2030 ESG goals, the plant will meet the highest standards for energy efficiency, environmental protection and a healthy working environment.

Let me now turn to our profitability. This first half, we have delivered CHF460 million of adjusted EBITDA, an increase of 25.3% year-over-year. This increase was driven by volume growth across the business, favourable product mix linked to growth in Fine Fragrance, as well as stronger margins in Taste & Beyond and in Ingredients. This, along with our proactive resource management and higher safety inventories, contributed to mitigate the impact of ongoing cost inflation in raw materials, energy and transportation.

Compared to prior year rates, foreign exchange had a favourable impact of CHF2 million on the adjusted EBITDA. Excluding this impact, adjusted EBITDA would have increased by 24.8% year-over-year.

Adjusted EBITDA margin as a percentage of revenue reached 20.5%, an increase of 2.1 percentage points compared to the previous year. Excluding the impact of foreign exchange, adjusted EBITDA margin would have increased by 2 percentage points over the prior year.

Looking first at Perfumery & Ingredients, revenue increased by 11.7%. This was driven firstly by industry-leading growth in Fine Fragrance, which has now surpassed pre-pandemic revenue levels, despite ongoing softness in travel retail.

We also continued to see strong momentum in Ingredients, which grew revenue by double digits. We benefited from the strong market demand in ingredients supported by our vertical integration and differentiating local supply in Europe and North America, as well as our strength in renewable ingredients.

Consumer Fragrances revenue declined by minus 0.3%. This was due firstly to a high comparable period last year, as consumer fragrances had achieved record growth at the start of the pandemic, while end-market demand is now softer. In addition, several mid to small customers have seen their production capacities impacted by shortages of raw materials and packaging, as well as logistical challenges, which in turn resulted in lower demand. Despite this context, we have achieved multiple customer brief wins. We have also been selected as core suppliers by several key customers.

Foreign exchange had a negative impact of minus CHF4 million on revenue, or minus 0.3 percentage points. As a result, revenue grew by 11.4% on a reported basis, reaching CHF1.495 billion.

Adjusted EBITDA increased by 22.5% year-on-year, to CHF308 million. This improvement was the result of the combination of higher volume, favourable product mix from Fine Fragrances as well as stronger margins in our Ingredients business, which had a favourable prior year comparable period. This offset the impact of ongoing raw material and energy inflation.

Foreign exchange had a negative impact of minus CHF2 million. Excluding this impact, adjusted EBITDA would have increased by 23.1% year-over-year. Adjusted EBITDA margin as a percentage of revenue was 20.6%, an increase of 1.9 percentage points. Foreign exchange had a negligible impact.

Moving now to Taste & Beyond, we delivered strong performance, with revenue continuing its track record of growth ahead of the industry, while also strengthening profit margins. Revenue increased by 13.4% year-over-year, with double-digit growth across all categories, beverages, sweet goods and savoury.

This is the result of our strategy of focused innovation in the categories that are driving industry expansion, following consumers' evolving needs and diet transformation. We grew revenue by double digits in innovations and beyond flavours categories, offering our customers superior integrated solutions in sugar reduction, in plant-based foods, in naturals and in nutrition.

At the same time, we have sharpened our commercial focus, gaining share with our partner customers and helping them win bigger in a rapidly evolving market.

Foreign exchange had a favourable impact of CHF3 million on revenue, or 0.5 percentage points. As a result, revenue increased by 13.9% on a reported basis, to CHF746 million.

Adjusted EBITDA reached CHF153 million, an increase of 31.4% year-over-year. This was driven by volume growth and cost discipline on commercial expenses, which more than offset ongoing raw material and energy cost increases.

Adjusted EBITDA margin as a percentage of revenue was 20.5%, an increase of 2.7 percentage points. Excluding the favourable impact of foreign exchange, adjusted EBITDA margin would have increased by 2.3 percentage points.

Turning now to cash generation, free cash flow reached CHF162 million for the first half of the year. This represents a decrease of 10.7% year-over-year. Our cash conversion ratio of free cash flow to reported EBITDA was 36%.

While we achieved a 47% increase in net profit year-over-year, this was offset by the working capital impact of an additional CHF117 million of change in inventory compared to the same period last year. We chose to prioritise customer service levels and security of supply at a challenging time for the industry and for our customers.

Other elements of change in working capital had a positive effect on free cash flow, highlighting our commitment to maintain a strong investment grade credit rating through solid cash generation.

And this leads me to my final slide. You can see here our leverage, using our estimate of the Standard & Poor's methodology. At the end of December 2021, our leverage reached a ratio of 3.0x, which compares to a ratio of 3.2x at the end of June 2021.

This steady deleveraging is explained by the following factors. Firstly, a decrease of CHF141 million in the value of the bond debt, linked to favourable exchange fluctuations against the euro. This also had a negative CHF24 million impact on the equity credit of the hybrid bond.

Secondly, an increase of CHF93 million in adjusted EBITDA for the past 12 months rolling, driven by topline growth and margin improvement. And thirdly, a reduction in net pension liabilities of CHF42 million, linked to the evolution of Swiss long-term interest rates, primarily.

These factors more than compensated a reduction in cash of CHF265 million, linked to the payment of dividend and the execution of our M&A strategy and a CHF13 million increase in other debt, mainly linked to our M&A commitments.

As we stated previously, we are fully committed to retaining a strong investment grade credit rating, as demonstrated in the favourable variation of our leverage ratio. I will now hand back to Gilbert for a few closing remarks.

Gilbert Ghostine

Chief Executive Officer

Thank you, Benoit. Before we open for Q&A, I would like to leave you with the following key messages.

We are off to a strong start in fiscal 2022, with double digit revenue and profit growth, despite ongoing challenges in raw materials, energy, supply chain and logistics.

We are achieving our ambitions, accelerating profitable growth, gaining share with our customers through focused innovation, intimacy, and superior service. All the while, we continue to lead the industry in responsible business.

We are seeing the success of our strategy of continued investment in our business, focusing on segments with high profitable growth potential, sharpening our commercial focus and accelerating our digital transformation.

Looking ahead, although we know that we will continue to face headwinds from the raw materials and supply chain environment in the second half of the year, we are encouraged by our industry-leading growth in the past six months. We will strive to continue delivering organic growth and share gains, bringing more innovation to market and balancing customer service with our commitment to deliver strong cash generation.

Thank you again for your interest in Firmenich and for your support. Benoit and I will be happy to take your questions.

Q&A Session

Diego Chantrain

We have a few questions that have been submitted over the webcast from Zurich Cantonal Bank, from Sven Bucher. The first one is could you comment on the elevated inventory level and how much are you above normal? In addition, did you have any special costs related to COVID, such as transportation or more temporary?

Gilbert Ghostine

Thank you, Sven, for this question. I will ask Benoit to answer it.

Benoit Fouilland

Thank you, thank you for the question. Yes, we had an increase in inventory levels, as we described in our prepared remarks. We had an increase of CHF150 million in the first six months of the year, which brings us significantly above our normalised level. We are close to a month of inventory ahead of our normalised level and this is a situation that we are monitoring very closely, always with a careful balance between ensuring safety of service for our customer and on the other hand, focusing on generating on our cash target.

Diego Chantrain

Next question from the same analyst, could you comment on the extent of the cost inflation in the first half and going forward, how and when can you pass on the higher cost to your customers?

Gilbert Ghostine

This is a question that is divided in two, on how and when would we pass the higher cost to our customers, we will pass it immediately. This is not an experience that we didn't have and face in the past. This is the market reality. We told you when we had the last call back in August that we see inflation creeping up and we are taking all the action in order to make sure that we pass this pricing to our customers. And our customers are dealing with the same situation almost, with the key raw materials that they are importing.

I think the key advantage that Firmenich brings here is that we are a value-added company, we are not about cost and this is delivered by the new technologies, by the new solutions, by the creativity and by the innovation that we bring to our customers and to the business.

On the extent of the cost inflation, we see this somewhere going in between the high mid-single digit and high - I would rather say high single digit, that's where we would see the cost inflation for the calendar year 2022.

Diego Chantrain

Gilbert, then we have a final question from Zurich Cantonal Bank. Why was the growth rate in Europe so much higher than the rest of the world?

Gilbert Ghostine

In Europe it's very clear. As you know, we are the most vertically integrated player in our industry in ingredients and we lead our industry in ingredients. So we are the leader of our industry in ingredients and the core manufacturing facilities that we have for ingredients are in Europe and that's where you look at our presentation, our growth in ingredients was at 24%.

The other element is fine fragrance. We are the number 1 in prestige fine fragrance in the world in our industry and the core of the prestige fine fragrance is in Europe and fine fragrance grew by 38%. So the combination of both these elements, with the strong performance that we had in our Taste & Beyond business, led to having 22% growth in our European operation.

Diego Chantrain

Thank you, Gilbert. It seems we don't have any further questions online at the moment, so let's give people a few moments to ask their remaining questions. If there are no further questions, we would like to in the name of Firmenich to thank you for your time and if you have any follow-up questions, please do not hesitate to send them to the Firmenich Investor Relations team.

Gilbert Ghostine

Thank you very much.

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