Firmenich Full Year 2021 Earnings Call

Presentation

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Head of Investor Relations

Good morning and welcome to the Firmenich full year 2021 earnings call for the year ended 30 June 2021. With us today are 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. Such forward-looking statements 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 those expressed in the statements contained 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 may also include 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 on an organic basis at constant currency, as defined in the alternative performance measurements pages.

With that, it is my pleasure to hand it over to Gilbert.

Gilbert Ghostine

Chief Executive Officer

Thank you, Diego. Good morning, everyone. I hope you are keeping healthy and safe. Let me begin by thanking you for your interest in Firmenich. We are pleased to present to you our full year results for our fiscal year 2021.

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

Let me turn first to the review of the past year. This year we delivered a solid set of results, despite the continued disruption caused by the pandemic. We achieved 4.7% revenue growth, with double-digit growth in many of our key markets and segments.

Our adjusted EBITDA margin as a percentage of revenue was 19.1%, a decrease of 3 percentage points compared to the previous year, caused by unfavourable impact of acquisitions and foreign exchange, as well as the effect of the pandemic on cost and product mix.

This year we delivered strong free cash flow of CHF511 million, an increase of 12.5% compared to the previous year, in line with our commitment to maintain a strong investment grade credit rating.

We saw a strong increase in momentum in the second half of the year, in both our perfumery, ingredients and Taste & Beyond divisions. We made further progress on integrating DRT, our largest acquisition to date. Despite the disruption caused by the pandemic, we saw a revenue rebound in the second half of the year, as well as improving profitability.

Turning to the year ahead, we see fiscal 2022 as a year of growth, leadership and excellence in execution. We will focus on gaining value market share by driving profitable organic growth, while continuing to deliver strong cash generation and ensuring safety of supply for our customers. At the same time, we will continue to raise the bar in ESG leadership, true to our longstanding culture of responsible business.

Let me delve into our performance highlights for the full year. We have delivered solid revenue growth across our business. In Taste & Beyond we continued the strong momentum seen since last year, growing by 5.2%. In Perfumery & Ingredients, we saw a strong rebound in fine fragrance, which closed the year up 8.9%. Ingredients also delivered double-digit growth, on the back of strong customer demand.

We delivered double-digit growth in our key geographies of North America, China and India. This demonstrates a strong execution in these markets and we are encouraged to continue to see such rapid growth in geographies where lockdowns have eased.

We also delivered double-digit growth in some of our key strategic initiatives, including sugar reduction, Agilex, our mid-market perfumery platform in North America and our e-commerce channel, which has passed the CHF200 million bar this year.

This year has of course not been without its challenges. We have seen a slowdown in consumer fragrances, which closed the year up 0.6%. This slowdown is linked to a tough comparison to the previous fiscal year, as well as increased competitive pressure in some of our markets.

In Europe, we close the year with a contraction of 0.7%, as a result of the impact of the pandemic on fine fragrance.

In the second half of the year, we increased our momentum across the business. Taste & Beyond growth accelerated to 6.7%. In Perfumery and Ingredients, fine fragrance rebounded by 39.0%, as restrictions linked to the pandemic were partly lifted in several geographies. Ingredients growth also accelerated further to 22.4%.

Turning to our key geographies, we continued to deliver double-digit revenue growth in North America, China and India. Europe rebounded to 8.6% revenue growth, driven by the recovery of fine fragrance. Latin America revenue contracted by 5.9% in the second half of the year, primarily linked to the slowdown in consumer fragrances.

The transformational acquisition of DRT, a leader in naturally derived renewable ingredients, enabled Firmenich to build the world's leading innovation platform for renewable, biodegradable and sustainable ingredients for the flavour and fragrance industry. This allows us to meet our customers' growing demand for sustainable products, which we see as a key long-term growth driver for our industry.

During the past year, the pandemic had an adverse impact on revenue and profit at DRT, due to lower demand in fine fragrance and the DRT industrial end markets. As a result, we are behind our original business case assumptions for this fiscal year. While ongoing short-term volatility remains, in the second half of the year, we have seen an encouraging revenue rebound, as well as improving profitability.

We continue to make progress on the integration and we are confident in the strategic fit of this acquisition and the long-term competitive advantage provided by our unique and proprietary access to renewable ingredients.

The pandemic has not stopped us investing in the future. Through our ongoing investment and focus on our strategic priorities, we are well placed to capture the growth opportunities as we exit the crisis. Let me highlight the key areas on which we have focused.

The first area is leadership in naturals. Demand for naturals, clean label and origin traceability is rising, with consumers increasingly focused on wellbeing and healthy food and beverage choices.

With our naturals platform, we're transforming our offerings with a portfolio of natural ingredients and innovation programs, with strong and distinctive technology. In the past year, we have added over 100 new natural ingredients to our palette, created with clean label in mind.

As a leader in naturals, we introduced FreshSlice, our new collection of natural citrus oils, delivering unique freshness and authenticity. We have continued reinforcing our commitment to an ethical, sustainable and traceable value chain, by establishing partnerships with SCA3P in Provence, on lavandin and with Authentic Products in Madagascar, on vanilla.

The second area of investment is accelerating our innovation and building on our proprietary technologies. We are proud of our leadership in science. We consistently invest a higher percentage of our revenue on R&D than our competitors and have over 4000 patents currently active.

As an innovation-led organisation, we aim to identify critical consumer trends and key societal challenges, such as sustainability, malnutrition and sanitation, where we can leverage our R&D capabilities to unlock opportunities for our clients. This leads us to invest and innovate in several high growth segments for our industry.

Let me give you a few examples of this. In Perfumery and Ingredients, we rolled out our DeodEcode technology, a breakthrough innovation capable of eliminating bad smells, across several consumer fragrances categories, contributing to double-digit revenue growth in malodour control solutions.

We are leading the charge for conscious perfumery, to minimise the impact of fragrance products on the environment. Our fragrance palette is fit for the future and continuously being improved.

Thanks to our digital tools, our perfumers have the information they need to create 100% biodegradable fragrances. Already today, over 45% of our fragrance sales consist of ultimately biodegradable fragrances.

In Taste & Beyond, our sugar reduction solutions achieved double-digit revenue growth in fiscal 2021, powered by innovations that allow unprecedented sugar reduction in dairy products, without the use of sweeteners, while keeping a natural sweet taste.

Addressing changing global dietary needs, we launched new flavour solutions that deliver a natural and authentic meat-like cooking and eating experience in plant-based meat analogues.

We also apply our innovation to natural ingredients. This fiscal year we launched a new range of natural extracts obtained by a revolutionary, sustainable proprietary extraction technology that enables us to process biomasses never previously used in the industry for natural ingredients.

As part of our accelerated digital transformation journey, we are proud to have launched this year both the world's first flavour and first consumer fragrance designed with the help of artificial intelligence.

We also launched ScentMate, the first artificial intelligence enabled platform aimed at entrepreneurs and independent brands. ScentMate streamlines and simplifies co-creation with these customers to deliver winning fragrance solutions, giving them immediate access to exceptional scents and making dedicated perfumers and experts available throughout the entire journey. We are very excited by the strong growth of this platform since its launch and would encourage you to check it out on scentmate.com.

The third area of focus is M&A and external partnerships. This year we have continued our strategy of targeted acquisitions, to complement our technological capabilities and increase our access to growing markets.

In Perfumery & Ingredients, we have increased our controlling stake in MG International, reinforcing our presence in the small-to-medium customer market in Turkey and the Middle East.

We also agreed to acquire a non-controlling stake in Essential Labs, a digitally native supplier of fragrance solutions to entrepreneurial businesses in the US premium home market, with a potential future path to control, depending on performance.

In Taste & Beyond, we increased our minority stake in ArtSci in China and reinforced our strategic partnership to serve local customers with increased agility and geographic reach.

As you know, Firmenich is the leader in responsible business in our industry. Our responsible business model is a core part of our family heritage and is consistent with our values and company purpose. The third party credentials that recognise our ESG performance are a source of trust for our clients and investors, as well as pride and motivation for all our colleagues.

Let me give you a few highlights. Firmenich is one of only two companies in the world to have received a AAA rating from CDP, in climate, water and forests, for the third year in a row. This is a testament to our efforts to address environmental issues through our operations.

This year we have also been rated for the first time by Sustainalytics, with a score of 8.6, which not only places us as ESG leaders in our industry and the chemicals sector, but also in the top 1% of over 14,000 companies rated worldwide.

In May, we received the global EDGE MOVE certification, recognising our work and commitment for gender equality. This is an upgrade of our earlier certification, which we obtained for the first time in 2018.

This year, we announced bold new ESG targets for 2025 and ambitions for 2030. We are taking the strongest carbon emissions commitment in our industry to reach carbon neutrality in our direct operations by 2025 and carbon positive impact beyond that date. By 2030, we will strive to achieve absolute carbon emissions reduction in line with the 1.5°C Science-Based Targets.

In line with our new goals, we are also improving further our ESG reporting standards.

Looking ahead, our fiscal year 2022 will be a year of growth, leadership and excellence in execution. As the global situation starts to normalise, the rebound that we saw in the last six months gives us confidence for the year ahead. We are particularly encouraged by the latest performance improvements in fine fragrance, in Europe and in DRT.

Over the next fiscal year, we will strive to accelerate profitable organic growth, further sharpening our focus on high growth segments and markets and leveraging our insights into changing consumer preferences to help our customers win bigger.

We will continue delivering breakthrough innovation, reinforcing our renewable portfolio with new proprietary fragrance ingredients. We will also introduce new differentiated food solutions and taste ingredients and keep leveraging our digitalisation to accelerate our transformation.

Consolidating further our leadership in natural, sustainable and renewable products, we will continue to expand our naturals platform, leveraging the vertical integration opportunities created by our acquisition of DRT and continue to lead the way in conscious and renewable perfumery.

Excellence in execution will be core to our success, providing best-in-class service and safety of supply to our customers, driving increased agility and simplification across our business model and keeping a sharp focus on profitability and cash generation.

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

Benoit Fouilland

Chief Financial Officer

Thank you, Gilbert and a good morning, everyone. Firmenich delivered solid full year results, with accelerating momentum in the second half of the year. Despite the continued challenges posed by the pandemic, we delivered 4.7% revenue growth. This was driven by solid growth across Perfumery & Ingredients and Taste & Beyond, with double-digit growth in our key geographies and strategic initiatives.

The acquisitions of DRT and MG International contributed CHF470 million, or 12.1 percentage points, to revenue growth. On a constant currency basis, revenue increased by 16.8% year-over-year.

The foreign exchange impact on revenue was negative CHF255 million, or negative 6.6 percentage points for the year. This follows the trend we reported at the first half results, with the appreciation of the Swiss franc versus some of our key trading currencies, including the US dollar, the euro, the Brazilian real and the Chinese yuan.

As a result of these effects, on a reported basis, revenue increased by 10.2% versus the previous year, reaching CHF4.272 billion.

Across our geographically diversified business, we have seen a solid rebound in revenue growth, especially in those markets where restrictions linked to the pandemic have eased.

By the end of the year, most regions had returned to growth. Let me look first at some of our key markets, where we have achieved double-digit revenue growth.

In North America, we grew by 11.3%. We achieved 14.4% revenue growth in China, which drove the growth of the entire North and East Asia region to 9.7%. In India, we grew by 17.4% and by 9.4% across the broader region of India, Middle East and Africa.

The pandemic has continued to affect some regions more than others in financial year 2021. In Latin America, revenue grew by only 1.3% for the full year, with a slowdown in the second half linked to consumer fragrances.

Growth in Southeast Asia remained flat for the full year, while in Europe revenue declined slightly by 0.7%. Both regions returned to revenue growth in the second half of the year.

Let me now turn to our profitability. In a challenging year, adjusted EBITDA declined by 5.0% to CHF816 million, due to the combined effects of acquisitions, unfavourable foreign exchange and the impact of the pandemic on costs and product mix.

Acquisitions contributed CHF47 million to adjusted EBITDA and foreign exchange had a negative impact of CHF80 million. If we exclude the impact of acquisitions and foreign exchange, adjusted EBITDA would have decreased by 1.1% compared to the previous year.

Adjusted EBITDA margin as a percentage of revenue was 19.1%, a decrease of three percentage points compared to the previous year. Acquisitions had a negative impact of 1.2 percentage points. Foreign exchange had a further unfavourable impact of 0.6 percentage points.

Excluding the effect of acquisitions and foreign exchange, adjusted EBITDA margin would have contracted by 1.2 percentage points. This is primarily due to the unfavourable product mix in Taste & Beyond, partly linked to the pandemic, as well as exceptional supply chain costs linked to maintaining safety of supply to our customers in this challenging environment.

Let me now cover the view by division. Looking first at Perfumery & Ingredients, revenue increased by 4.4%. This was driven firstly by the recovery in fine fragrance, which rebounded in the second half of the year, reaching pre-crisis levels in the fourth quarter.

Fine fragrance had been significantly impacted over the past 18 months by the retail closures and travel restrictions linked to the pandemic in many geographies and so this recovery in the fourth quarter is very encouraging.

We also saw accelerating momentum in ingredients, which grew by double-digits on the back of strong customer demand in both natural and synthetic ingredients.

In Consumer Fragrances we experienced a slowdown, with the segment growing by only 0.6%. This is firstly linked to a tough financial year 2020 comparative period. Let's remember, at the beginning of the pandemic, consumer fragrances achieved record growth, driven mostly by global customers and the body and home care categories.

This effect has now slowed down and in some cases eroded, particularly in the second half of the year. In addition, we have faced increased competitive pressure in Latin America.

The contribution of acquisitions to Perfumery & Ingredients was significant this year. Including the impact of acquisitions, which amounted to CHF470 million, or 19.1 percentage points, revenue increased by 23.5% year-over-year at constant currency.

Foreign exchange had a negative impact of CHF171 million, or 7 percentage points. As a result, on a reported basis, revenue grew by 16.5%, reaching CHF2.855 billion.

Adjusted EBITDA increased by 3.3% year-over-year to CHF550 million. Acquisitions contributed CHF54 million and foreign exchange had a negative impact of CHF59 million. Excluding the impact of acquisitions and foreign exchange, adjusted EBITDA would have increased by 4.2%.

Adjusted EBITDA margin as a percentage of revenue was 19.3%, which corresponds to a decrease of 2.4 percentage points. Acquisitions had a negative impact of 1.7 percentage points and unfavourable foreign exchange had an impact of 0.8 percentage points. Excluding the effect of acquisitions and foreign exchange, adjusted EBITDA margin would have increased by 10 basis points compared to the previous year.

Moving to Taste & Beyond, revenue increased by 5.2%, driven by strong growth in beverages and dairy, supported by our capabilities in sugar reduction solutions. This more than offset the negative impact of the pandemic on other categories, including food service.

From the onset of the pandemic, we launched deep consumer insights surveys across 22 countries to anticipate changing consumer needs. Those needs have changed rapidly, with higher expectations on what food and beverages should deliver and we have worked with our customers to help them adjust their innovation pipeline.

Moving first to develop these consumers insights clearly differentiated us in financial year 2021, enabling us to develop increased intimacy with our customers and in return allowing us to better align our innovation to fuel growth.

We achieved double-digit revenue growth in the key markets of China and India, as well as mid-single digit revenue growth in North America. This robust performance was enabled by our deep consumer insights, by our innovation-led client service and by the strength of our external partnerships with ArtSci and VKL.

Foreign exchange had an unfavourable impact of CHF84 million, or 5.9 percentage points on revenue. As a result, revenue decreased by 0.7% on a reported basis, to CHF1.417 billion.

Adjusted EBITDA decreased by 18.5% to CHF266 million for the full year. This decrease was the result of the combined impact of unfavourable product mix partly due to changing consumption patterns during the pandemic and exceptional supply chain costs incurred to ensure business continuity and avoid disruption to customers during the crisis. It was also caused by raw material price fluctuations on vanilla. In addition to this, foreign exchange had a negative impact of CHF21 million.

Adjusted EBITDA margin as a percentage of revenue was 18.8%, a decrease of 4.1 percentage points in comparison to the previous year. The adverse impact of foreign exchange accounted for 0.4 percentage points of the total.

Important to note that we've seen sequential adjusted EBITDA margin improvement in the second half of the year, as some of these pressures on profitability have started to ease.

Turning now to cash generation, free cash flow increased by 12.5% year-over-year to CHF511 million. This translates to a strong cash conversion ratio of reported EBITDA to free cash flow of 59%.

This cash conversion was achieved primarily through disciplined working capital management. Our free cash flow also benefited from the one-off cash effect of asset disposals for CHF42 million and the settlement of legal claims for CHF30 million. These two exceptional effects contributed approximately four percentage points to our cash conversion ratio.

Our strong cash generation is consistent with our commitment to retaining a strong investment grade credit rating through solid cash generation, which leads me to my final slide, the discussion of our financial position and leverage.

Using the S&P leverage calculation methodology, our leverage reached a ratio of 3.2x at the end of the fiscal year 2021. This compares to a ratio of 3.5x at the end of December 2020.

The decrease is explained by the following factors. Firstly, our strong cash generation, which resulted in an increase in cash on hand of CHF111 million. Secondly, a reduction in other debts of CHF110 million. This reduction is linked to a reduction in bank overdraft regarding DRT, as well as a decrease in short- and long-term borrowings.

Thirdly, a decrease in net pension liabilities, linked to updated demographics assumptions following the publication of a new mortality table, as well as an increase in the discount rate due to the evolution of Swiss long-term interest rates and higher than expected actual return on plan assets.

Finally, a decrease of CHF28 million in adjusted EBITDA. This is principally linked to DRT, which as we discussed experienced a soft start to the year, in addition to a tough comparison to pre-COVID results. It's important to remind that those pre-COVID results were included in the pro-forma figures shown at the half year results presentation for the calculation of leverage.

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.

So now let me hand back to Gilbert for a few closing remarks before taking your questions.

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. First, we are proud of what we have achieved in fiscal 2021. Despite the continued challenges of the pandemic, we delivered solid mid-single-digit revenue growth, in line with our CAGR for the previous strategic cycle.

We have increased our customer intimacy, differentiating ourselves through deep insights on rapidly evolving consumer trends, focused innovation and superior levels of service.

We have continued to invest in our business, focusing on segments with high profitable growth potential, strengthening our leadership team and accelerating our digital transformation.

All of this gives us confidence that in fiscal 2022, we are well positioned to build on our increasing momentum, to further drive organic revenue growth, expand our profitability and continue delivering strong cash generation.

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

Q&A Session

Diego Chantrain

While we wait for questions from the phones, we have two questions from the online platform from Sven Bucher in Zurich from Zürcher Kantonalbank. First one is where do you see [wide spots] regarding M&A, more technology or more or different customer segments?

The second question is could you give more insight on the integration of DRT, which areas are you behind in your plans and what will it take to close the gap?

Gilbert Ghostine

These are two very good questions. Let me deal with the first one, the first one on M&A. Our strategy has been very clear over the last four or five years, we focused and channelled all our M&A focus behind three key areas. The first one is naturality, the second one is technology, complementary technology and the third one is geographic expansion and broader reach into key strategic markets of US, India and China. We see this strategy still relevant for us for the years to come.

Now, let me move to the next question. Regarding your question on DRT, integration in DRT is working according to plan. The challenge we have has nothing to do with integration; it is mainly driven by the perfect storm of external factors due to the pandemic. If we look at the DRT business, 30% to 40% of the DRT business is mainly coming from investment in materials.

So here you're talking about adhesives, construction, [tires] and these three industries were very impacted negatively during the pandemic. Another component is fine fragrance and you know that fine fragrance was also impacted negatively during the pandemic. Now the good news on DRT is that we have either defined more synergies than we have initially expected when we did our homework.

On the flipside of it, we had some additional challenges on the operations where we saw that they were underinvested in their operations, mainly on the safety standards. And that's an area where we will use the additional synergy to entrust them to bring their safety standards up to our standards. But we are confident in the recovery in DRT based on the rebound that we saw in the second half of the year.

Diego Chantrain

The next question is from Gianmarco Migliavacca from Neuberger. Can you please quantify the impact of DRT on EBITDA and also quantify underperformance versus your original plan?

Benoit Fouilland

As we highlighted in the previous remarks, the impact of acquisition on the profitability of the adjusted EBITDA level was equivalent of 120 basis points of margin deterioration. And that impact is entirely coming from DRT, because in fact MG was slightly accretive to our EBITDA margin.

With respect to the underperformance versus the original plan, we are not disclosing the original plan, but to give you a qualitative answer, clearly we have had a soft start with DRT in the first half of the year, where there was a profitability at EBITDA level during the first of the year - the first part of the year was negative.

Why what we've seen on the second half of the year, which is very encouraging, is a strong rebound of the top line which has also translated in an improving profitability. So based on what we've experienced in the second half of the year, we feel confident that we can get onto the trajectory of our original plan of profitability margin level in the very close future.

Diego Chantrain

Thank you, Benoit. The next question comes from Robert Jaeger in Amundi. Can you discuss raw material cost development over FY22?

Benoit Fouilland

Thanks for the question. As you all know, this is your last topic of focus in the entire industry. And we've taken into consideration in our plan an increase of raw material both linked to the increase of the brand, as well as the overall inflation that is currently being experienced on the market.

What we think there is still uncertain, there are still a lot of questions as to what exactly would be the impact. But we feel comfortable that we have lots of levers in order to mitigate the various scenarios that could happen on the raw materials during the course of 2022. Also on the pricing side, as well as on the raw material pallet side, always working in the close partnership with our clients.

Diego Chantrain

Thank you, Benoit. We have two questions from Schroders. The first one is why is the combined revenue and EBITDA in FY21 including full year of DRT?

The second one is what is the guidance and revenue growth in EBITDA margin that you can give for fiscal year 2022?

Gilbert Ghostine

Very good, thank you for these questions. Look, first on DRT, we don't disclose the breakdown of these businesses and anyway, you can't compare it with the way it used to be with the private equity, because we were the biggest customer of DRT and a significant part of their net revenue [went into] the transfer price in terms of financing.

Now moving to future views, when we had issued our bonds we told you that we report twice a year, we're fully transparent, but we will not give future guidance. But what I can tell you is a message of confidence and based on the rebound that we have seen in the second half of our fiscal year 2021, we are well positioned to further drive profitable organic revenue growth and expand our profitability and continue our strong cash generation in fiscal 2022.

Benoit Fouilland

If I may, Gilbert, I want just to clarify one point on the first question. I want to make clear that the acquisition closed on 1 June last year, we so have the entire - in the combined financials of financial year 2021, we have a full year of DRT to be included, so just to clarify this point.

Second aspect, when assessing the impact of DRT on the overall financials of the Company, you need to keep in mind that the first half was significantly impacted by COVID. And as we said, in the second half we have seen a strong rebound with double-digit growth on the top line as well as a need for [inaudible].

Diego Chantrain

We don't have any further questions from the web platform or on the line at the moment. If you would like to take the opportunity to ask further questions, please do so at this point.

Gilbert Ghostine

Okay, we don't have any new questions, so I want to thank you for your commitment and your support for Firmenich. Any questions you will have, feel free to channel it through Diego and definitely Benoit and I will get back to you as quickly as possible. Thank you very much for your support and I wish everyone on the call a happy summer holiday, that is very well deserved. But please stay vigilant, stay safe, because the pandemic is still out there. Thank you.

[End]