

Full Regular Transcription

Cloetta

Q3 2024 Results

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COMPANY REPRESENTATIVES

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Katarina Tell – CEO and President

Frans Rydén – CFO

PRESENTATION

Lindholm Laura

A warm welcome and thank you for joining Cloetta's Q3 Interim Report presentation. I'm Laura Lindholm, the Director of Communications and Investor Relations. Our CEO, Katarina, and CFO, Frans, will first go through our results, after which we will move to the Q&A, where you either have the possibility to dial in and ask questions live, or alternatively, post your questions through the chat. The chat will open up for questions when the Q&A starts. Over to you, Katarina.

Tell Katarina

Thank you, Laura. This is my first complete quarter as CEO of Cloetta, and today I am proud to present a strong quarter with both continued organic growth and strength in profit. But first, over to the agenda.

Today, it looks as following. I will start with a brief company overview and then move to our Q3 highlights. Then our CFO, Frans, will walk you through both our Q3 and year-to-date financials. After that, I will highlight a few things related to our strategic priorities. And as always, we wrap up with a Q&A.

In case our new shareholders have joined the call, I would like to provide a brief description of Cloetta. We are a leading confectionery company in Northern Europe, and we are proud how our loved brands and products bring joy to memorable occasions. We are convinced that our consumer focus is the basis for us to grow and our leading brands to flourish. I have more than 2,600 colleagues at Cloetta, and we have sales in more than 60 countries. Sweden, where I was area president before assuming my current role is our largest geographical market, followed by Finland, the Netherlands, and Denmark.

In terms of product categories, candy is our most significant one, followed by chocolate. Pastilles and chewing gum stands for a bit less, 15% of the portfolio, but are important categories as they continue to add to our profitable mix. We focus on developing leading brands. Ten of our brands account for over 50% of our net sales, and we have two reporting segments. Branded packaged products is what the name implies, all our packed branded products. Pick and mix is candy and natural snacks that are picked by consumers and are primarily sold through our CandyKing brand and concept.

As previously mentioned, we had a strong quarter. We continued organic growth and strengthened profits, and I like to highlight some key takeaways.

Our organic growth continues, and in Q3, we delivered 2.2 billion SEK in net sales, which is equal to 5.7% organic growth, while we also continue to strengthen the profit. The total volumes were stable, whereas pick and mix grew faster than the branded products. As mentioned in Q2, pick and mix as a category is the fastest growing confectionery segment in the Nordics.

And talking about profit, I am super happy that our rolling 12-month adjusted operating profit was the highest one ever. The profit was improved versus Q3 last year, and this was primarily driven by continued margin enhancing activities in pick and mix. We are flagging the Q2 report of the potential impact of the historically high cocoa price during the second half of this year, but the cocoa price did not significantly impact this quarter. I'm happy to also share that net debt over EBITDA is, again, well below our long-term targets and landed at 1.6.

Now, it's always time for the financials, and I'll hand over to Frans, who will walk you through both our Q3 and year-to-date financials.

Rydén Frans

Thank you, Katarina. For the quarter, as Katarina mentioned, again we're delivering growth and a very significant 5.7% organic net sales growth on the back of continued solid 1.4% branded packaged growth, which is well in line with our long-term target of 1 to 2%, and pick and mix almost 19%. Now, I'm going to comment on the pick and mix growth when we look at the segments in detail, but I want to point out that our total growth is not against a weak comparator of Q3 2023. Q3 2023 was actually the first quarter for Cloetta to deliver above 2 billion in quarterly sales. This is growth on top of that. This is the fifth consecutive quarter with sales above 2 billion and this 2 billion, 196 million is actually our highest quarterly net sales ever, beating the prior record, which was the fourth quarter last year.

Before looking at the segments, I want to comment on the effect of the sale of the Nutisal brand. In Q2 this year, we had two months of Nutisal in the quarter, and now we have none. The record net sales I mentioned is despite the loss of that. And then to understand how our continued business is doing, when I say organic growth, I mean our ongoing business, excluding Nutisal. In accordance with the relevant accounting standards, comparable numbers have not been restated for the sale of the brand. And going forward, you will also continue to see that we report sales on the nuts category, given that we will continue to sell nuts as part of the pick and mix assortment.

Now, let's look at the segments. On the top, as mentioned, branded packaged sales grew organically by 1.4%. And again, that growth is coming on stable, underlying volumes.

I think we're down maybe 100 tons on almost 22,000 tons sold. And again, we're seeing the power of our great brands that people love and trust. We have continued to invest in our core brands while securing fair pricing, and the stable volumes are one effect of that. And I'll come back to the investment.

For the pick a mix segment on the lower half of the slide, 18.6% growth is driven by strong volume growth and continued margin enhancing initiatives. And on top of that growth, as a result of the absence of last year's negative one-timer, when our large retail customer, Wilko, in the UK, went into administration. That gives this year's net sales growth versus last year a boost in comparison. But the key takeaway here is that we are reporting our highest absolute sales ever for pick and mix.

Looking then at the profit, and regardless if we're looking at the quarter or the year-to-date number, there is a strong step-up on the operating profit in absolute terms for the quarter to 238 million. Now, 238 million SEK is one of the highest quarterly profits ever. And as Katerina mentioned, with this quarter, we are delivering the highest rolling 12 months' profit, and we're doing that hands down. Now, the quarterly profit step-up is driven by margin enhancing initiatives in pick and mix on top of the strong growth I mentioned, full stop. That explains the step up.

And as we always do, on the next slide, and I'm not going to move there quite yet, when I show the results by segment, it will be really clear. But before going there, there's four comments I want to make on this overall picture that I think will be helpful.

First, I mentioned the solid volumes, but here in the graph on the left-hand side, the volume/mix block looks flattish or even negative. Now, that is the effect of pick and mix outgrowing the branded packaged sales, and that we have a continued challenge on the pastilles and gum categories. This is, of course, an area where we will continue to focus and with further potential upside going forward. Because this is an upside that is not requiring us to reach some never-before-seen levels, but rather to continue to reduce the gap to where we have been in the past, which is obviously more attainable.

Secondly, we are still working through the details with the long-term supplier related to the isolated case of a raw material quality deviation, which we spoke of in both quarter one and quarter two. The quarter three results are not aided by our supplier making good on that.

Thirdly, in Q3, we have seen cost inflation stabilise, although we also flagged earlier that the higher cocoa price levels would affect us in the back half of the year. We do have some of that effect in the quarter, but we will only see the full effect of those higher costs in our results in quarter four. Mitigating action is ongoing, and we have taken further pricing at the end of quarter three, but those higher costs will make delivering a third consecutive 10-plus percent margin in quarter four, let's call it a good challenge for us, including with the compression effect of a fair pricing approach.

And with respect of the fair pricing or compression, which is my fourth point, the margin remains compressed as a result of the input cost increase. And I've illustrated this before, and I'll do it again. If we have a product that's produced for 50 and we sell it for 100, we get 50 in profit and a 50% margin. Now if the cost goes to 70, and as a result, we take the selling price to 120, the profit will remain 50, but the margin drops to 42. And that effect is still in our numbers as we have priced for cost. But if you look at the middle column here, where it says price versus cost, it actually looks very, very favourable at plus 42 million. And that's why we need to look at the next slide with the segments separated.

In this slide, this is what illustrates what I mentioned. For the branded packaged products on the top row, we're just about holding the profit stable. While we did take further pricing in the quarter, and we did see some of the effect of higher cocoa prices I mentioned, there's obviously no pricing here above fair pricing. Instead, the variance to last year does include this year's step-up in investments behind our core brands. I mentioned in Q2 that we would add 10 to 20 million, and we landed at the higher end of that range. Now, that investment helps protect the volumes in the quarter, and it adds to our brand strength also long term. But we're, of course, not content with lower profitability, and we will continue to work hard on rebuilding that through growth, mix, portfolio rationalisation, net revenue management, cost control, you name it.

Now, looking at the lower row, it is clear here that the total Cloetta step-up in profit in the quarter came from pick and mix. Here, we deliver yet another quarter in line with our margin target of 5 to 7% adjusted. We worked for a long time really hard on correcting the profitability in pick and mix. And for an equally long time, almost, a lot of that was not visible externally due to the increasing input cost. But now we have three consecutive quarters with profitability in the range of the target of five to seven. Given all our margin enhancing activities, like pricing, volume growth, efficiencies in merchandising, product assortment, fixtures, etc.

Now, the variance versus last year is also helped by the absence of last year's Wilko bad debt that I mentioned, but that is just a variance. The absolute profit this quarter and the profitability, that is

what it is, and that is not helped by last year's issue with Wilko. If anything, this quarter's good result is despite that we lost Wilko a year ago. We are very, very pleased to report these numbers for the segment.

Let's move down to sales, general and admin. The increase, as it has been for a number of quarters, is driven by general salary inflation relating to our workforce. And also the same effect for our suppliers, including work contracts often are indexed, but also importantly, the planned higher marketing spend that I mentioned. Overall, we are managing to offset the higher costs in the rest of the P&L. And importantly, the spend as a percent of our sales is lower now in Q3 than it was in the first half of the year. Nonetheless, this is an area where we are also further increasing our focus to ensure we spend only where matters the most, and that we can get the most bang for our bucks.

With respect to the marketing spend, given the step-up now in Q3, and as investments were already strong in Q4 last year, I can flag that we do not see a need for a similar year-over-year increase in the coming quarters, as we did for this quarter or for the prior quarters this year. On the longer term, while we are happy with the strong, well-deserved profit, we are not taking our eyes off the need to continue to drive also operating profit margin. And as pleasing as it is to report another quarter of double-digit profit, and despite the quite significant compression effect that I mentioned, there is some way to go before our target of 14%.

Now, with pick and mix solid in green, we continue to work on our other opportunities. And given the decision to put the greenfield on hold and reassess the project and the alternative options, we will, of course, come back in due course in quarter one 2025 on that.

Now, there is a seasonality to our cash flow, where historically, most of the cash is generated in the back half of the year. But as we exited quarter two, we were already, year-to-date, 148 million better than last year. I'm really pleased to report that our Q3 free cash flow of 211 million is also stronger than last year, bringing the year-to-date total to 236 million better. As mentioned in Q2, these numbers do not include any of the proceeds from the divestment of the Nutisal brand, and that comes on top. Part of the improvement is due to the efforts to increase the focus on cash generation across our organisation, and part is due to the inflation having slowed down and with working capital not increasing despite the increased sales.

On the CapEx, 38 million is on the lower side of our normal, due to several contributing factors, including phasing of spend, and to some extent, driven by the preparation for the greenfield, given that the investment there would or will also help us avoid, or rather displace, the need for other CapEx in other plants. Nonetheless, for my final slide, I'm really, really pleased and proud of our

team that, on account of the strong cash flow, we closed the quarter with a net debt EBITDA of 1.6, well below our target of 2.5.

And for those who do the detailed match, the leverage is actually ever so slightly below 1.6, even lower than it was in Q1 this year. And then looking at the graph on the bottom left, that red line there is our leverage. And as you can see, it has consistently been trending downwards to improve position the last three years. And the bumps are Q2 when dividends are paid, but even so, for Q2 this year, the bump was hardly discernible, which puts us in a gradually better place quarter after quarter after quarter.

Finally, we currently have access to additional unused credit facilities, commercial papers, and cash on hand of 4 billion SEK, of which less than half, €160 million are facilities made available for the greenfield, which is now on hold. For yet another quarter, I conclude that our financial position is strong. And with that, back to Katarina.

Tell Katarina

Thank you, France. Now I would like to give a few highlights related to our current strategic priorities. First, I would like to start with an update on the greenfield plant project. Most of you likely know that in Q3 we announced that we will put the greenfield project on hold to reassess the plans and other options. The reassessment was initiated due to the increased risk related to the energy supply, which also impacted on the timing of the plant start-up.

I also personally believe it was the right time to reassess the project, since it's still in an early phase, and the investments are so far relatively limited. The reassessment of the greenfield project will be done in the light of everything that has changed since 2022, and our ambition is to accelerate profitable growth. I also want to emphasise that there are opportunities in our network to compensate for the volumes that in the mid-term were planned to be produced by the greenfield.

Another strategic priority is to optimise our product portfolio. During the quarter, we have strengthened the profit, mostly through module [?] enhancing activities in pick and mix. We have for several years also focussed on an efficient product portfolio. Key objectives are to discontinue products with lower profitability and harmonise recipes and formats. Since the baseline 2021, we have reduced the number of stock keeping units by 30%, and we have already exceeded the targets we set out as an annual target for 2024.

Then a bit more about how we grow our top brands. An important part of growing our brands, and specifically our packed business, is through new occasions and moments. And I would like here to

share two very good examples. The first one is Skipper's Pipes in Denmark, where we last year launched the iconic count line product as mini pipes in bags.

By these actions, we are reaching 77% of the Danish market instead of only 7%. And consequently, the brand consideration for Skipper's Pipes has also increased with 29%. You can also see the effect on the volume.

For those of you not familiar with this, the higher brand consideration is simply that the consumers would consider buying a brand to a larger extent than before. The second example is Tupla, our most well-known count line chocolate in Finland. The Tupla brand has, in August this year, stepped into the ice cream category through licensing and is therefore reaching new consumers. Surprisingly, since, living in the very north, have one of the highest consumption of ice cream per capita in the world. But that is also because it's also consumed as a dessert.

That concludes this update. And we will now move over to the Q&A.

QUESTION & ANSWER

Lindholm Laura

Thank you very much, Katarina. Thank you, France. It's now possible to either dial in and ask your question live, or, alternatively, post your questions to the chat. And we know that we already have some questions in the chat. Maria, do we have any questions on the line?

Operator

There are no questions on the line.

Lindholm Laura

Thank you very much. We move over to the chat. The question is from Danske Bank. You mentioned the Swedish candy trend in the USA. Can you elaborate on what you see and how it affects you? Is it a market you will invest more in, and what are the M&A potential going forward?

Tell Katarina

I can take that answer. First of all, pick and mix is building on the trend of consumers looking for more individualisation, as they pick the candy according to their personal preferences. And it's been very strong in the north and now we also see in other markets as well the demand. From a Cloetta

perspective, as you know, we have for several years been struggling with poor profitability on the pick and mix.

And we are now very proud that we have been able to make the turnaround and take the pick and mix from loss making to first breakeven, and now we actually have, for the third quarter, delivering on a good profitability, as we have said in our targets. Now is actually the time for us to evaluate, to take the next step. First, we wanted to make the current business sustainable and profitable, and now we're ready to take the next step. That's where we are now.

Lindholm Laura

Thank you very much. And then we move to the pre-registered questions. This one is from For You [?]. What are the alternative options to the greenfield?

Rydén Frans

First of all, the reason that we're doing the reassessment is because when we approved this in 2022, a lot of stuff has happened. And, as also Katrina mentioned, we haven't actually put shovel to the ground yet, so we haven't started building anything, so it's a good time to revisit this. But also, back in in 2022, we were already sharing some of the options we looked at that time to do internally what we could do internally and with contract manufacturers, if we could buy additional capacity outside.

We talked about greenfield in various locations. There was a whole range of options, and we presented some of those during the Capital Market Day. All of these, we will, of course, go back and revisit now. Things have changed, but we have also learned a lot during this project. As you know, we closed one of the plants in Rosendahl this summer, which originally it was envisaged it could only be closed once the greenfield was up and running. But we learned a lot, and we could go ahead and do that and move forward. There could also be other opportunities within our existing network. We'll reassess all of it and come with what is the best solution for Cloetta.

Lindholm Laura

Thank you, Frans. Maria, any questions on the line?

Operator

No, Laura, there are no questions.

Lindholm Laura

It appears we don't have any questions from the line, so we take the opportunity to conclude the events and remind everyone of our upcoming IR event for our next report in Q4 is published on 29th January.

But before that, on 14th November, we have a plant visit to our Ljungsbro plant in Sweden. Which is, as you know, the home of iconic brands such as Ahlgrens bilar, Kexchoklad and Polly. The visit is arranged by Danske Bank, and this morning we still had a few seats left. If you would like to join us, please call Danske Bank, they will arrange that for you.

Before we meet again we, of course, also hope that you get the chance to enjoy Cloetta's products during many joyful and memorable occasions.

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