Haleon Q3 Trading Update

Thursday, 2nd November 2023

Introduction

Sonya Ghobrial

Head of Investor Relations, Haleon

Welcome & Disclaimer

Good morning everyone, and welcome to Haleon's conference call for our third quarter trading statement. I am Sonya Ghobrial, Head of Investor Relations. I am joined this morning by Tobias Hestler, our Chief Financial Officer

Just to remind listeners on the call that in the discussions today, the company may make certain forward-looking statements including those that refer to our estimates, plans and expectations. Please refer to this morning's announcement and the company's UK and SEC filings for more details, including factors which could lead to actual results to differ materially from those expressed in or implied by any such forward-looking statements. Today we plan to run through some slides before opening the call for Q&A. For those listening to our webcast who would like to ask a question you can find the dial in details on page two of today's press release. As you know, whilst the focus today is on revenue performance, we have also provided Group profit and margin details on both a reported and an adjusted basis, with a full reconciliation including for organic revenue growth in our appendix. For information, we do not intend to provide quarterly profit data on an ongoing basis and will only do this for as long as Pfizer reports our results as part of its financial statements and until our registration rights agreement with Pfizer and GSK terminates.

With that, I would like to hand the call over to Tobias.

2023 Third Quarter Trading Statement

Tobias Hestler

Chief Financial Officer, Haleon

Thank you Sonya, and good morning everyone. Let me first start with our third quarter highlights. As you will have seen from our release this morning, we had a good third quarter, with 5% organic revenue growth, split 6.6% price and a 1.6% decline in volume mix. This performance was underpinned by continued share gains across our business.

Across the quarter, growth was driven by a number of categories including continued strength in both Oral Health and Pain Relief, and it is encouraging to see VMS back to growth. Respiratory also had a good quarter with normal seasonal cold and flu sell-in. Digestive Health saw good consumption growth, but our results were negatively impacted by one off inventory movements from some US retailers. The latter was the primary driver for the volume mix decline in Q3.

Equally important, we saw continued good operating leverage, with inflationary cost pressures more than offset by price and efficiencies across the business, resulting in operating margin expansion of 90 basis points.

On the back of today's strong numbers, I am pleased to reiterate that we remain firmly on track to meet our full year guidance to grow organic revenues by 7-8% and operating profit 9-11 % constant currency resulting in margin expansion.

Finally, its worth highlighting that we closed the sale of Lamisil in the last couple of days, earlier than we expected, you will recall that we announced the sale of the brand with our half year results. This demonstrates our commitment to optimise the portfolio through active brand management.

Q3 Key Financials

Turning now to our third quarter results. Revenue of £2.8 billion reflected 5% organic revenue growth. Adjusted operating profit was up 8.8% constant currency, resulting in a 24.6% margin, up 90 basis points constant currency. As expected, the adverse impact of FX was most pronounced in the third quarter due to year on year strength in Sterling against the US Dollar and the movement in a number of emerging market currencies which negatively impacted margin at actual rates.

Looking at the drivers of revenue growth in more detail.

Q3 2023 Revenue Growth

Strong organic growth driven by pricing

We delivered 5% organic sales growth comprising 6.6% price and a 1.6% decline in volume mix.

Pricing in the quarter included some incremental price as well as the carryover of pricing taken over the last twelve months. As I have said previously, we will continue to take price as needed, and remain confident in our ability to do so given the strength of our innovation and brand and market positions, albeit going forward this will be at a lower level than seen so far this year.

In Q3, we also had a one point benefit from high inflation economies - Turkey and Argentina.

We saw continued volume/mix growth in APAC and in our Oral Health business, although overall, this was offset by two factors: One – the anticipated decline in Emergen-C where the category has reverted towards pre-pandemic levels which has now stabilised; and two – the one off retailer inventory stock reduction in Digestive Health in North America. Here we had an inventory build last year following a temporary supply shortage which we have now lapped and saw some US retailers reduce their inventory this year. Importantly, consumption in Digestive Health continues to see good growth. Excluding both these impacts, volume mix would have been flat across the Group and, I would expect improved volume mix in the fourth quarter compared with what we have reported for Q3 today.

Turning now to our performance across the categories.

Good growth across categories

Continued strength in Oral Health

Looking at the quarter, I was particularly pleased that Oral Health revenues grew 9% with healthy growth in price and volume mix. Sensodyne was up double digit underpinned by continued share gains, benefiting from innovation and strong growth across a number of markets including India and Japan, as well as good performance in the US.

VMS is back in growth with continued strong performance of Centrum which more than offset the expected decline in Emergen-C.

The double digit revenue growth of Centrum was driven by positive price and volume mix helped by geographic expansion and activation in a number of markets.

Pain Relief also delivered good revenue growth, up 6% with Panadol driven by strength in Middle East and Africa, and Voltaren growth which was underpinned by performance in Europe from new innovations. Advil declined mid-single digit largely due to more competitive market conditions.

Respiratory revenue was up 4%, with strong growth in Theraflu and Robitussin from sell-in ahead of the cold and flu season which more than offset both, the lower out of season use of cold and flu products and a decline in Flonase following a weak allergy season.

Altogether, this demonstrates the strength and the diversity of our portfolio, delivering 5% organic growth for the Group.

Let me now move to look at geographic segment performance.

Strong emerging market growth

Looking across the regions, we saw slightly differing trends from one region to another, with strong growth across EMEA and Latin America, and Asia Pacific, and a slight decline in North America.

Our emerging markets saw 11% growth, which included a benefit from pricing taken in high inflation economies. Emerging markets made up a third of our revenues and included double digit growth in India and broad-based growth in other emerging markets.

Developed markets grew 2%.

Looking at each region in more detail - starting with North America

North America

Strength in Oral Health offset by retailer inventory adjustments in Digestive Health

Organic revenue declined 1.5%, with a 2.6% price increase and a 4.1% decline in volume mix. As I mentioned earlier, this decline in volume mix largely reflected two factors – First: a one-off reduction in Digestive Health brand inventories from retailer stocking movements and second: the expected decline in Emergen-C. Excluding both these impacts, volume mix would have been slightly positive.

Across the categories, we saw mid-single digit growth in Oral Health led by Sensodyne underpinned by consumption and new innovations including Pronamel Active Shield.

VMS increased low single digit with strong performance of Centrum that more than offset the decline in Emergen-C where demand has now stabilised.

Centrum benefitted from the activation of cognitive function claims on Centrum Silver and the launch of our Pre-Natal blends.

Pain Relief declined mid-single digit driven by Advil.

Respiratory health was down low single digit: with growth in Cold and Flu offset by a decline in allergy products due to a weak season resulting in inventories being run down to normalised levels.

Finally, Digestive Health and Other fell mid-single digit largely due to a double digit fall in Digestive Health revenue – as I already explained.

Turning to Europe, Middle East, Africa and Latin America.

EMEA & LATAM

Strong performance with volume/mix weakness in Latin America

Organic revenue increased 10.8%, split 12.7% price and a 1.9% decline in volume mix. As you'll recall, this region is the most exposed to higher inflation economies – Turkey and Argentina which had a 3% impact on organic growth.

The decline in volume mix was driven by Latin America where volumes declined double digit from weakness in Colombia and Mexico which was more than offset by strong pricing.

Looking across this segment, there was strong growth in Middle East and Africa helped by Panadol. In Europe, revenue was up mid-single digit with broad based growth, including strong results in Germany.

Across the categories, Oral Health saw double digit growth largely driven by Sensodyne and denture care. We are seeing good consumer uptake for a number of brand innovations including Parodontax Active Gum Repair.

In VMS, the region saw a low single digit decline driven by some Local brands. Having said that, Centrum was up strongly helped by continued activation and strong execution in markets across the region.

Pain Relief revenue was up double digit reflecting strong growth from Panadol, and a number of successful campaigns featuring our specialist ranges and growth in Voltaren.

Respiratory sales increased in the mid-single digit range driven by price and the sell in of Cold and Flu products ahead of the season. We continue to drive innovation in this category and recently launched Otrivin Nasal Mist which delivers an improved consumer experience through both comfort, ergonomics and efficacy.

Digestive Health and Other saw sales up double digit with good growth across most of our brands.

Finally, turning to Asia Pacific.

APAC

Balanced price and volume/ mix growth

Organic revenue increased 5.9%, with 2.9% from price and 3.0% from volume mix.

China, our second largest market overall, was up mid-single digit after a very strong first half following the easing of Covid related lockdown restrictions, leaving China up mid-teens for the nine months. Elsewhere, India grew double digit and Australia and New Zealand was up low single digit.

Within the categories, Oral Health saw high single digit growth, underpinned by strong growth in Sensodyne particularly in India, Japan and China.

In VMS, we saw low-single digit growth helped by successful consumer campaigns for Centrum partly offset by a decline in Caltrate.

In Pain Relief - Voltaren saw strong growth particularly in China and Australia. As expected, Fenbid revenues declined after extraordinary strong growth in China during the first half and we have ensured inventories have returned to more normalised levels.

Respiratory revenues were up double digit driven by strong growth in Theraflu.

Adjusted operating profit growth

+8.8% at constant exchange rates; +60bps operating leverage

Turning now to our operating performance.

Adjusted operating profit was up 9% constant currency driven by positive operating leverage.

Looking at the bridge in more detail, standalone costs were 10 million lower than last year as we run down our TSAs with GSK.

I'm pleased to report strong execution with pricing and efficiencies offsetting inflationary cost pressures and negative volume, resulting in positive operating leverage. Importantly, we ensured continued investment in consumer facing A&P which grew ahead of organic growth.

Finally, as expected, there was a £100 million or 140 basis points headwind from material movements in foreign exchange on a translational basis which particularly impacted the quarter.

Taken together, this resulted in a 5% decline in Adjusted Operating profit at actual exchange rates and a 24.6% margin. As a reminder, Q3 is typically our higher margin quarter in the year given advanced sales of cold and flu products ahead of the season.

This takes our year to date adjusted operating profit constant currency growth to 9% and a margin of 23%, up 10 basis points constant currency.

Outlook

For full year 2023

As I mentioned earlier, we are pleased to reiterate confidence in our full year outlook.

We continue to expect to achieve organic sales growth of between 7-8%.

We see another year of positive operating leverage and expect adjusted operating profit to grow between 9-11% constant currency. This will therefore result in adjusted operating margin expansion on a constant currency basis.

Conclusion

So, to sum it up. Haleon has delivered a strong third quarter performance demonstrating the strength and diversity of our portfolio, and execution across our markets.

We delivered 9% adjusted operating profit growth at constant currency and strong positive operating leverage across the business.

As such, we have re-iterated our full year guidance.

Given the momentum across the business in what remains a challenging market environment, we remain confident of delivering on our medium-term guidance, as we stated in this morning's results release.

With that, I would like to hand back to the operator to open up for questions.

Q&A

Rashad Kawan (Morgan Stanley): Good morning Tobias and Sonya, thanks for taking my questions. A couple from me please. The first one on the negative volume mix in EMEA and LATAM. You talked about the decline largely a function of weakness in Mexico and Colombia. Can you get into that a bit more? What is driving that? Is it increased elasticity as a result of price increases, more competitive dynamics with peers? Any colour there would be helpful. Then the second point you are calling out the one-off retailer inventory adjustment in Digestive Health in North America which means obviously it is material enough. Can you quantify that? Is that something that you would expect to reverse into Q4? Thank you.

Tobias Hestler (Chief Financial Officer, Haleon): Sure, thanks Rashad. First on LATAM, I am not concerned about the overall price/volume pricing dynamics. Overall we have seen LATAM had a strong quarter, up double-digit in revenue. When you look at Colombia they still had a Covid wave in Q3, so they are cycling over that. I think in Mexico it has more to do with shipments of cold and flu that are different between the quarters this year. Nothing particularly concerning to call out. I believe the team in LATAM has done a really good job and keep pushing up pricing in a very dynamic environment but also maintaining overall the ability to hold volumes.

On North America there are two things. First of all the decline in Digestive Health is the biggest driver of why volumes were down, not only for the North American market but also for the Group overall. That is the primary driver. What made Q3 a bit bigger is because last year we had built inventory because we had an out-of-stock situation that we had to re-pipe inventory and build. There was an inventory build last year. This year there was an inventory burn because some retailers decided to hold a little bit less inventory at the beginning of the quarter. Most importantly, consumption is still strong. When you look at those half-year and also the Q3 numbers consumption on these products is still up, which is the most important thing. I do not expect that to reverse. It is hard to predict what retailers are doing but this will not repeat or come back in Q4 from our perspective.

Rashad Kawan: Perfect, thank you Tobias.

Guillaume Delmas (UBS): Good morning Tobias and Sonya. Two questions from me as well please. The first one is on VMS. Tobias, can you shed a bit more light on the various brands' development in Q3? It seemed that Centrum, your largest brand there, accelerated very nicely from low-single digit in Q2 to double-digit in Q3, but then Emergen-C remained a drag, Caltrate was unusually weak and the local brand in EMEA LATAM had another soft quarter. First, in terms of category growth are you seeing an improvement in VMS? Then is it fair to assume that now that Emergen-C is fully normalised and that I would assume Caltrate should be back to growth in Q4, that VMS could very soon be back to its medium-term growth range ambition of mid-to-high single digits? Then my second question is on your multi-year organic sales growth guidance of 4-6%. I appreciate it is early days, but can you already confirm that your ambition is to achieve 4-6% next year in 2024 despite the uncertainty around the Respiratory division and the tough comps in China? Thank you.

Tobias Hestler: Thanks Guillaume. Let me start with VMS. You pointed our Centrum so feel really strong about this brand. Geographic expansion, activations, activating on the clinical trials and the claims that we are rolling out globally. I think the brand is really strong and overall it was pleasing to see that VMS is back to growth. Then you mentioned there were few of the local brands, for example Polase in Italy which is more of a seasonal brand with a very mild summer in Italy so there is a bit of ups and downs on those. We are not wildly concerned about these brands. Also we have a VMS brand in Russia that we stopped distributing so would not be too concerned about those. Then Caltrate was also more of a one-time thing - the distributor change in China and then last year Southeast Asia was very strong. Again, I think not concerned about Caltrate, particularly not for China where the biggest market is.

On Emergen-C what is good to see over the last few months is that consumption has now stabilised. It stabilised pretty much at the 2019 levels in units and then you have on top of that the innovation and the pricing we did. It has been stabilised and it is now following the pattern where it was pre-Covid. Of course it is going to take us two more quarters to land there so we fully cycle over it, but I think it is good to see that it is found the place at 2019 and now going into the season it is starting to grow again. I think that will be behind us I would say in the not too distant future. And moreover with VMS I think we remain confident in the category, and it is back to growth now, so we had two strong years of growth in VMS. Now it is coming back with Emergen C down but Centrum more than making up for that.

Then on your multi-year question, yes we will guide for full year with our full year results but for us the 4-6% guidance is an annual guidance. This is our ambition that we grow 4-6% every year and not just over a several-year period. That is the first thing. The other piece is if we take a step back at half year we guided for 7-8% for the full year. That is 4-6% in the second half. We are right in the middle on that growth guidance with what we delivered in Q3, and we are very confident in our guidance and being in this guidance range for the year as well, given the strength of the portfolio, of the business that we have and the continued ability to take price as well.

Guillaume Delmas: Thank you very much.

Tobias Hestler: Thanks Guillaume.

Celine Pannuti (JP Morgan): Good morning Tobias and Sonya. My first question is a follow-up on what you just said in terms of the pricing. You said the ability to take price, but I think early on in your commentary you were talking about going forward a lower level of pricing than we have achieved this year. Can you talk about what kind of underlying pricing now we should be looking at? Then maybe is there any commentary you can make on costs that you are facing this year and how 2024 cost is shaping up. My second question is on volume. You are guiding for volume to improve in Q4. If I take out the impact of the one-off issue in Digestive in the US I get to -0.6 volume at the Group level. Is that the ballpark of what we should be aiming for in Q4? Then in 2024 maybe coming back on the previous question on that volume point. We are seeing this unwind of volume that you benefitted from in 2022 so here as well do you expect that unwind to be an issue in the first half of the year?

Tobias Hestler: Good, thanks Celine. On pricing when you look at what we did in Q2 we had the peak in pricing. It was 7.9%. It came down to 6.6% in Q3, as I had said at half year. I would expect that trend to continue. Now, it does not mean we are not taking any pricing. The team continues to take pricing. Of course clearly in the emerging markets where there is a high inflation environment but we also for example took more price in the US since September of mid-single digit to low double digit on about a quarter of the portfolio. I think we feel good about our ability to take price. Also we have seen limited price elasticity to-date so from that point we need a reassurance of our ability to take price and doing that going forward. Now, of course we are mindful of the consumer backdrop. I think when you look what the team has done, we found the good spot between pricing and volume but of course we have got to be responsible in the pricing we are taking overall in this environment.

On the cost inflation I think we are down into the mid-single digits so that is clear. There are a few of the commodities starting to come down but then I think there are others that are still staying stubbornly high. For example, sugar or anything that is sugar related but also I think the bigger topic right now is labour costs and how labour costs evolve. Again, what we said before with pricing, I think we should have the ability to offset inflationary headwinds with the price that is coming through.

Then on your volume question, for us as I said it is going to be better than Q3 was. When you look at Q4, the puts and takes, last year there was a recall that helped. We do not expect to have a recall this year. Then of course the other direction is last year Fenbid in China and Contac that took off after the change in Covid strategy in China. Then we had a very early peak on the cold and flu season in the US. As I have guided at half year, we still expect volume to be down on cold and flu in the second half of the year, particularly in Q4 as well given that dynamic. However, if you can take a step back from it in aggregate for the business very confident about the 4-6% guidance we have given for half two. That then puts us very well into the 7-8% range.

Then going into next year I think it is exactly the same comment. You have seen we did 5% growth in Q3 with ups and downs, and with puts and takes. The beauty of this business in my view is the diversity of its portfolio from a brand perspective. You saw the high-single digit, nearly double-digit growth on our power brands that carried us forward. The strength across four categories that carried the growth. Then also the geographic mix with a good third of the business being in emerging market versus developed markets. I think that gives us the ability and the strong confidence that we can grow and continue to grow in this 4-6% range going forward.

Celine Pannuti: Thank you.

Tobias Hestler: Thanks Celine.

Karel Zoete (Kepler Cheuvreux): Good morning all, thanks for taking the question. I have two questions. First one is basically a follow-up on China. You already provided some insights, highlighting the difficult comparison base for the Pain franchise. How should we look at the coming quarters ahead? Is that going to be something where you would anticipate therefore a decline or are there also offsets in China? The other thing is on the US Pain franchise. You mentioned Advil was down mid-single digits and regarding Voltaren you particularly mentioned the progress in the European markets. How is the brand doing in the United States? Thank you.

Tobias Hestler: I did not get your last one. I got China, the Pain portfolio, Advil US but then you said something about Voltaren.

Karel Zoete: Yes, Voltaren. Yes, you highlighted that Voltaren is doing well in Europe and that is good. Probably an improvement in Germany too but how is Voltaren doing in the US?

Tobias Hestler: Okay, good, thank you. I got it. Let me start with China. Let me first explain a little bit what happened on Fenbid. In China there was the second Covid wave in May. That was over May/June. Then the government in China expected another third wave so they told retailers and pharmacies to keep stocking product. That did not happen so luckily for our colleagues in China, ultimately we then decided during the third quarter to ramp inventory down to a normalised level given there was no another wave. Now, last year of course you had the big pickup in Q4 and Q1 so we would expect the drag from that on the Pain Relief portfolio. However, when you look at the rest of the portfolio in China I think we have very strong brands. We see continued growth in the Oral Health business, in the Caltrate business and in the rest of the portfolio. Yes, there is going to be a bit of a drag on the Pain Relief China business as we cycle that over but overall feel good about our ability to grow the Chinese business.

On Advil in the US there is a very competitive situation. Of course Advil's key competitor is Tylenol. They have done very well so I think we have got a bit of work to do now. Nothing surprising in a big portfolio like we have. Pain Relief overall grew 6%. All the brands did well in that. Even with the small drag that we had from Fenbid and then Advil was down. A key focus for us is to put attention to that. We just took a price increase on it which will support but yes I think it is one of those where we go head to head with a very strong competitor.

Then I think on Voltaren overall this year we have seen good growth on the brand in aggregate. It is doing well in the US. It has done particularly well in Europe now coming off a higher use of systemic pain relief products. That helps Voltaren because in times when people use a lot of tablets they tend to reduce the use of topical pain relief medicine.

Karel Zoete: Thank you.

Chris Pitcher (Redburn): Thank you very much, I have got a couple of follow-ups and a question. Tobias, are you able to say what the China growth would have been ex the destocking impact of Fenbid and Contac? I appreciate it is going to be an issue in the next couple of quarters. Just to get the underlying growth there. Then on the question about volume growth into Q4, can you give us a bit of colour about the mix effect you would expect within that? Particularly with potentially lower Respiratory sales. Then an underlying question on India. You highlight the strength of Oral Health, but can you say how Digestive Health performed and how the rollout of Centrum is doing? Thanks.

Tobias Hestler: Yes, China overall has grown so I really do not want to go into the ups and downs. Ultimately I think the China performance overall is strong. The Fenbid was a small drag there on both the Pain Relief category globally but ultimately what the team has been doing they have offset these impacts very well so far. The good news is we have a broad portfolio in China that carries us through.

On Q4 yes as you mentioned as part of our guidance we would expect volumes to be down in Respiratory. Now, this is an assumption, so we need to see what the season does but I think that is clear. There is going to be another drag clearly on Fenbid because that is when the consumption started. Then when you look at Digestive Health and others there should be a small help because last year we had a recall on Tums. That is probably the biggest puts and takes in the portfolio. Then of course you have to remove Lamisil from the model as well. I know it is small, but I think we closed that a bit earlier than we expected. Then I think the rest of the portfolio we expect continued strong momentum and performance.

Then you asked about India.

Sonya Ghorbrial (Head of Investor Relations, Haleon): I think on India what I would say in Digestive is strong, double-digit so doing particularly well in the market and in the quarter.

Chris Pitcher: The rollout of Centrum still going to plan?

Sonya Ghorbrial: Yes.

Tobias Hestler: Yes.

Chris Pitcher: Thanks.

Tobias Hestler: Thanks Chris.

Tom Sykes (Deutsche Bank): Morning everybody. Firstly just on the gross cost savings of £300 million, I wondered if you could maybe just give us an update on when those should hit the P&L and perhaps how much of the £150 million to be clear you would expect to spend in full year 2023? On standalone costs, will there be any difference in seasonality in full year 2024 versus 2023 like there has been obviously in 2023 versus 2022? If I can, just a quick one, is there any part of your VMS business that has seen a GLP1 impact at all? Do you expect an impact of people taking vitamin supplements at all if they start embarking on taking those medicines? Thank you.

Tobias Hestler: Thanks Tom. On the cost savings we said the impacts are going to be in 2024 and 2025. We are making good progress, so we made announcements. Given the announcement largely impacts populations in Europe, we are in the middle of the ren-consultation phase, so it always takes a bit of time then for the savings to realise. As per labour law we have in those countries, you have to get consultation before people can exit the company. From our perspective we have made good progress on that, but we will expect the savings to hit in 2024 and 2025.

On the standalone cost that is now stable, and we are just ramping down now the TSAs. They were not a big amount but year-over-year you get the small benefit and I think that is going to be complete quite soon. From that point of view this is history, and I would hope that from next quarter on I do not need to talk about standalone costs anymore because they are in the base. There is no phasing. There is nothing to worry about that going forward. I put it in the bridge now even if it is only £10 million because it was such a topic before but that is going to be history now very soon.

Then on your GLP1 question we do not think we have a direct impact from GLP1 from consumers potentially changing behaviours. Ultimately we believe it is a good thing if people want to take care of their health and want to live healthier. That should be an overall benefit for us in my view, but I do not think there is any direct impact. It is also way too early to tell what it could do but I do not see any direct consequences on our business at this point.

Tom Sykes: Okay, thank you.

Sonya Ghobrial: We can just finish there with a couple of quick comments.

Tobias Hestler: That is good. Thanks everyone for your time and your interest in Haleon. As you have seen, we had a good quarter. I look forward to updating you on our progress next year together with Brian. If you have any questions, please do reach out to our IR team and it is also worth mentioning we will be hosting our first Haleon Highlights Mini Deep-Dive that will be on Oral Health on 7th December in London. We will also webcast that. Thank you and bye, bye for now.

Sonya Ghobrial: Thank you very much.

Tobias Hestler: Thank you.

[END OF TRANSCRIPT]