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Coloplast A/S (CLPBY.DK)

Q1 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Welcome to the Coloplast Interim Financial Statements for Q1 2021/2022. Throughout the call, all participants will be in listen-only mode and, afterwards, there'll be a question-and-answer session. Today, I am pleased to present Kristian Villumsen, President and CEO; and Anders Lonning-Skovgaard, Executive Vice President and CFO. Please begin your meeting.

Kristian Villumsen

President & Chief Executive Officer, Coloplast A/S

Good afternoon, and welcome to our Q1 2021/2022 conference call. I'm Kristian Villumsen, the CEO of Coloplast; and I'm joined by our CFO, Anders Lonning-Skovgaard; and our Investor Relations team. We will start like we usually do with a short presentation by Anders and myself, and then open up for questions.

Please turn to slide number 3. I'm very satisfied with a solid start to the year amidst the ongoing pandemic. We delivered 6% organic growth, a 32% EBIT margin before special items, and a return on invested capital of 43% after-tax and before special items. Broadly across all markets, we continue to take share and help more people with intimate health care needs.

To start off, let me just go through a few highlights from our quarter. Europe delivered 6% organic growth, driven by solid growth across all business areas. The Chronic Care business in Europe continues to post improved

growth, driven by an increase in growth in new patients. Wound Care delivered an impressive 17% organic growth in the quarter, also mainly driven by Europe.

Emerging markets, excluding China, delivered another solid quarter. The growth was broad based and driven by Ostomy Care in Russia and Latin America. And Interventional Urology growth was impacted by a high baseline in Men's Health in Q1 last year, but the underlying growth in procedures across regions was satisfactory.

Today, we are updating our full year guidance to include the acquisition of Atos Medical. The acquisition is targeted to close at the start of next week, on January 31st, as all relevant regulatory approvals have now been received. Atos Medical adds a new long-term growth compounder to Coloplast in a category with significant untapped market potential. Atos Medical is expected to grow 8% to 10% organically, with an EBITDA margin in the mid-30s and contribute to Coloplast's Strive25 financial guidance of 7% to 9% organic growth and plus 30% EBIT margin.

We're very excited to welcome the teams at Atos Medical and TRACOE to Coloplast and to start our growth journey together. Anders will take us through all the details later, but overall, on our financial guidance for the year, we're maintaining our organic growth top line of 7% – of around 7%, and we now expect a reported EBIT margin before special items of around 31% from previously around 32% due to amortization charges in connection with Atos Medical.

Before we dive into the results, just a few words on Omicron and the outlook for the year. The spread of the Omicron variant has impacted our end markets during January. We're seeing a few different effects, including some impact on new patients growth in Ostomy and Continence Care. Hospital access has been reduced especially in North America, France, and the UK with the number of hospital admissions due to COVID has increased. Labor shortages among healthcare workers is also putting some strain on hospitals.

We expect, though, that the impact of Omicron will be short-lived and, therefore, in terms of impact on our outlook, it's unchanged. We are, of course, monitoring the situation closely. And we do expect to see a slower start to Q1 in Interventional Urology, but the business has demonstrated during the pandemic that it can bounce back quickly; and, therefore, we're still optimistic on the full year.

Importantly, Coloplast continues to fully meet demand with all global manufacturing sites operating normally in terms of production and supply chain. Overall, we're encouraged by the continued recovery in Europe, the strong performance in emerging markets outside of China. Our Wound Care and Interventional Urology businesses are expected to deliver in line with our Strive25 ambitions.

We're still challenged in our US Continence business where the growth in new patients has not yet fully normalized. Similar to what we saw in Europe, intermittent catheterization treatment and bowel management treatment has been deprioritized, as these treatments can be postponed and there are alternatives. We expect growth to improve in the second half of the year as the growth in new patients normalizes.

We also continue to see some weakness in China related to the COVID-19 flare-ups and economic uncertainty, which continues to impact consumer sentiment. We believe that the dynamics in US Continence Care and China are transitory, and we continue to focus on our commercial initiatives and investments that will drive growth beyond the pandemic.

Now, let's talk about the results in more detail. Please turn to slide number 4. In Ostomy Care, organic growth was 6% for the first quarter, and growth in Danish kroner was 9%. Growth continues to be driven by our SenSura Mio

and Brava supporting products. Our SenSura and Assura/Alterna portfolios continued to post solid growth in emerging markets. At the product level, SenSura Mio Convex was the main contributor to growth.

From a geographical perspective, Europe was the key contributor to growth, led by the UK, France, and Spain. Growth in emerging markets was driven by Russia and LATAM. China contributed to growth, but was impacted by a high baseline in Q1 last year and weak consumer sentiment which is impacting the average value per patient negatively.

In Continence Care, organic growth was 5% for Q1 and growth in Danish kroner was 8%. Growth continues to be driven by the SpeediCath ready-to-use intermittent catheters with a good contribution from the SpeediCath Flex portfolio, as well as SpeediCath Compact and standard catheters. From a geographical perspective, sales growth was mainly driven by Europe, led by the UK and France. The US contributed to growth, but was negatively impacted by baseline and lower growth in new patients.

In Interventional Urology, organic growth was 5% for the first quarter and growth in Danish kroner was 8%. Growth in the quarter was driven by Women's Health in the US as procedural volumes improved further. The Endourology portfolio in Europe also contributed nicely to growth. Growth in Men's Health was slightly negative due to a high baseline in Q1 last year. Procedural volumes in Men's Health were healthy throughout the quarter, until the last few weeks in December when Omicron began to cause some cancellations.

In Wound & Skin Care, organic growth was 12% for the first quarter and reported growth in Danish kroner was 15%. The Wound Care business in isolation delivered 17% organic growth for the first quarter. The Biatain Silicone and Biatain Fiber portfolios were the main contributors to growth, driven by Europe; and, in particular, Germany, France, and Spain. The strong quarter for Europe also reflects some phasing. Emerging markets also contributed nicely to growth. Growth in China was held back somewhat by COVID.

With this, I will now hand over to Anders, who will take you through the financials and outlook in more detail. Please turn to slide 5.

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

Thank you, Kristian, and good afternoon, everyone. Reported revenue for the first quarter increased by DKK 431 million, or 9%, compared to last year. Organic growth contributed around DKK 288 million, or 6%, to reported revenue. Foreign exchange rate had a significant positive impact of DKK 131 million, or around 3% on reported revenue, as expected due to the appreciation of the British pound, US dollar, and Chinese yen against the Danish kroner. The appreciation of the US dollar and the British pound accounted for approximately 70% of the positive currency impact.

Please turn to slide 6. Gross profit for the first quarter amounted to around DKK 3.5 billion, corresponding to a gross margin of 68%, on par with last year. The gross margin was positively impacted by leverage and production cost and savings from the Global Operations Plan 5. On the other hand, the gross margin was negatively impacted by double-digit wage inflation in Hungary, increasing raw materials, and energy prices, as well as ramp-up costs at our new volume sites in Costa Rica.

The optimization program which is a key component of the Global Operations Plan 5 remains on track, and will contribute to maintaining a flat level of blue collar workers while ramping up the volume site in Costa Rica. The gross margin includes a positive impact from currencies of around 30 basis points.

The distribution-to-sales ratio for the first quarter came in at 29%, compared to 28% last year. Distribution costs increased by DKK 182 million, or 14%, compared to last year, which reflects increased travel and sales and marketing expenses as COVID restrictions eased; but also continued in commercial investments in the US, Interventional Urology, and consumer and digital initiatives. The admin-to-sales and R&D-to-sales ratio for the first quarter came in at 4% of sales, on par with last year. During the first quarter, Coloplast incurred special items of DKK 34 million related to transaction costs in connection with the acquisition of Atos Medical.

Overall, this resulted in an increase in operating profit before special items of 7% for the first quarter, corresponding to an EBIT margin before special items of 32%, on par with last year. The EBIT margin contains a positive impact from currencies of 50 basis points, mainly related to the appreciation of the US dollar and British pound against the Danish kroner. The EBIT margin after special items was 31%. Net profit after special items increased by 6% compared to last year.

Please turn to slide 7. Operating cash flow for the first quarter amounted to around DKK 1.1 billion, compared to around DKK 1.2 billion last year. The negative development in cash flows was mainly due to a decrease in trade payables and financial items, partly offset by income tax paid and increase in operating profit. Cash flow from investing activities was impacted by investments of around DKK 200 million in the first quarter compared to around DKK 1.2 billion last year. Excluding acquisitions, investments amounted to around DKK 300 million last year.

As a result, the free cash flow for the full year, there was an inflow of DKK 930 million compared to an outflow of DKK 14 million last year. Adjusted for the acquisition of Nine Continents Medical, the free cash flow was an inflow of DKK 936 million, down 1% compared to last year. The trailing 12-month cash conversion for the first quarter was 90% and the net working capital amounted to 25% of sales at 31st of December 2021 compared to 24% at the end of September 2021, mainly due to a decrease in trade payables due to timing. We expect to be around 24% for the full year.

Now, please turn to slide 8. As Kristian explained earlier, we have updated our financial guidance to include the impact of Atos Medical. The acquisition is targeted to close on January 31st and, therefore, an eight-month impact is included. Organic revenue growth guidance is unchanged at around 7%. The key assumptions behind our organic growth are also unchanged. Overall, we assume a continued resumption of hospital activities across our business areas.

For the Chronic business, the assumptions by region are as follows. For Europe, we expect continued improvement in growth, now that the growth in new patients has largely returned to pre-COVID levels. In the US, our guidance assumes a continued improvement in growth driven by gradual normalization of growth in new patients back to pre-COVID levels, especially in the Continence Care, which has been more severely impacted.

In emerging markets, our guidance assumes broad-based double-digit growth. China is expected to remain impacted by COVID-19 and economic uncertainty, which has impacted consumer spending. Our smaller businesses, Interventional Urology and Wound & Skin Care, are expected to deliver in line with Strive25 ambitions. We have no current knowledge of significant healthcare reforms that will impact 2021/2022.

In terms of phasing, I still expect growth to accelerate in the following quarters, driven in part by baseline, as well as improved performance in the US and China. Due to the positive currency development, our reported growth guidance in Danish kroner is now expected to be around 9% from previously around 8%. The impact of Atos Medical acquisition on reported growth for eight months is expected to be around 6 percentage point. So in total, reported growth in Danish kroner is expected to be around 15%.

For 2021/2022 we now expect a reported EBIT margin before special items of around 31% from previously around 32% due to around DKK 200 million in amortization charges related to an eight-month impact from the Atos Medical acquisition. The reported EBIT margin after special items is expected to be around 30% and is impacted by DKK 150 million in special items related to one-off transaction and integration costs related to Atos Medical.

The gross margin is expected to be positively impacted by operating leverage and efficiency gains through the Global Operations Plan 5. The gross margin will be negatively impacted by cost inflation, including a mid-single digit increase in raw material prices and double-digit wage inflation in Hungary, as well as increasing energy prices. On raw material, the key pressure on prices is coming from plastics and paper. Raw material prices have not increased further since November, but the higher prices are expected to remain for the duration of 2021/2022.

Fortunately, some of the additional headwinds on the gross margin will be offset by price increases and the positive impact from currency based on current exchange rates. Overall, I expect our gross margin to be in the low end of around 68%. The EBIT margin guidance also reflects an increase in operating costs related to the resumption of business activities, as the impact of COVID-19 recedes, as well as some pressure on freight costs. Overall, I expect that the operating costs will grow in line with or slightly below our reported revenue growth.

The EBIT margin guidance also reflects additional incremental investments, up to 2% of revenue, for innovation as well as sales and marketing purposes. This year, we're investing incrementally in all business areas and regions with a key focus on the US, Europe, emerging markets, and digital initiatives.

We now expect our net financials to end the financial year 2021/2022 at around minus DKK 200 million from previously minus DKK 150 million. Including Atos Medical, we expect our net financials to end the year at around minus DKK 350 million. The additional DKK 150 million is related to DKK 50 million in financing costs for bank and underwriting fees and around DKK 100 million in interest costs on the debt financing of Atos Medical where we are assuming an interest rate of around 1%.

CapEx guidance for 2021/2022 is around DKK 1.3 billion from previously around DKK 1.2 billion due to the impact from Atos Medical CapEx and integration CapEx related to the acquisition. Our effective tax rate is expected to be around 23% from previously 22% to 23%. The tax rate is positive impacted by the increased deductibility on R&D cost in Denmark, partly offset by one-off tax payments related to the acquisition of Atos Medical.

Please see our earnings announcement from today for a summary of all the key financial assumptions for Atos Medical during the Strive25 strategy. Thank you very much. Operator, we are now ready to take questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] And our first question comes from the line of Patrick Wood at Bank of America. Please go ahead. Your line is open.

Patrick Wood

Analyst, Bank of America Merrill Lynch

Q

Perfect. Thank you very much and thank you for taking my questions. I'll keep it for two for now, please. The first one, really interesting on the price increases side. I'm just curious roughly where you guys have been taking those and where you've sort of managed to do it? Given it's a relatively reimbursed market, felt like that might have been a difficult thing to get through. So just curious, a little bit more details on the price increases and where those are.

And then just, I guess, on the second slide, any update on the development of the new product launches or the clinical data in the background running on the Ostomy and on the Continence side. Just curious if there's any update to either timeline or what we're seeing there? Thanks.

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

All right. Hi, Patrick. It's Anders here. Let me start with your first question related to price increases. So, it is something we have been focusing quite a bit on recently in order to see how much of the headwinds we have on the raw material price we can pass on. And we are able to pass on some of the headwind, especially within IU and some of our businesses here in Europe and also across some of our business in emerging markets. So, it's a little bit broad based, but we are able to pass on some, but not the full headwind that we are seeing across the raw material price increases. Kristian?

Kristian Villumsen

President & Chief Executive Officer, Coloplast A/S

A

Then, Patrick, to your question on the things that we have in the pipeline, we are, if you will, off to the races in UK and Germany with the pilots that we have for our digital Ostomy solution. Just as a reminder, this is a new-to-world type of product and, therefore, the pilots are really to demonstrate value and finding a path to reimbursement. The pilots will run over the next 12 months, and you should expect to hear back from us by the end of that period. And depending on result will trigger investment and further expansion from that product. So, that's probably the first thing that you'll hear about.

It's a bit clinical year for the group, Patrick, overall. So, we're doing clinical work now around the new catheter platform. We're very excited about that platform. Like I've said previously, we're still on track to launch that in the first half of the strategic period. And on the new Ostomy platform, we're also in clinical work. That will launch in the second half of the strategic period. And then we've also begun the clinical work on the Nine Continents acquisition. That's basically started here in January. We're starting to enroll patients. And that work will proceed over the probably the coming two years. So, that will give you a sense of where we are in a sense of timing.

Patrick Wood

Analyst, Bank of America Merrill Lynch

Q

Super. Thanks for the details, everyone.

Operator: Thank you. Our next question comes from the line of Hassan Al-Wakeel of Barclays. Please go ahead. Your line is open.

Hassan Al-Wakeel

Analyst, Barclays Capital Securities Ltd.

Q

Thank you for taking my questions. I have a couple please. So firstly, could you talk about your expectations for the second quarter when it comes to Interventional Urology and Wound as it relates to the impact from Omicron, and whether we should expect any sequential weakness? And do you see any meaningful risk to your high single-digit expectation in IU based on what you are seeing today?

And then, secondly, could you please detail the gross margin impacts from FX, wage inflation, and raw materials in the quarter, and how do you see this playing out over the course of the year? And then if I can just squeeze one in on – relating to EBIT margins. Just on your comment around the lower end of gross margin, is there any meaningful offset in the SG&A line that should support EBIT margins? Thank you.

Kristian Villumsen

President & Chief Executive Officer, Coloplast A/S

A

Thank you, Hassan. Let me start with the first one, then Anders will talk to your question on margin. So, on Interventional Urology, the dynamics are such that we are expecting Q2 to be soft given what we've seen in January. So, we saw impact from Omicron already starting late in Q1, and we've seen that continue here into Q2. So you should expect a softer Q2. We're still confident that, that business is going to bounce back and we have seen it bounce back before.

So it is, of course, affected when surgeries are canceled. But once we get through Omicron particularly in in the US, we expect it to bounce back, and we still expect high single-digit growth for the full year. Wound Care, we are expecting Q2 to be softer than Q1, probably primarily due to a higher baseline. But for the full year, we still expect to grow significantly faster than the market.

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

And then, Hassan, on your questions around our gross margin and our full year EBIT margin guidance. So if we should start with the gross margin, as I said earlier, our gross margin in Q1 had a positive impact from currencies in the level of 30 basis points, and the negative hit went from raw material price increases, salary increases a bit higher than that. But overall, our gross margin for the quarter is more or less as we had anticipated when we started the year.

When we look into the remaining part of the year, I am looking at a bit higher raw material price increases. I'm also looking into higher energy prices. So, that's why we are now saying that the raw material prices in combination with the energy prices and the higher salary levels are going to impact our gross margin, something around 100 basis points. And that means that we will be around 68%, but probably in the low end when we look at the full year guidance.

And then your comment around the cost; so I'm expecting that our total cost base will increase at or slightly below the top line growth. I'm actually expecting that this quarter due to Omnicom and less travel, less sales and marketing activities, we will have a lower spend than we actually anticipated. But for the year, I'm expecting a slightly or at the reported growth level, and that gives me before special items an EBIT margin of around 31%.

I hope that answered your question.

Hassan Al-Wakeel

Analyst, Barclays Capital Securities Ltd.

Q

That's very clear. Thank you.

Operator: Thank you. Our next question comes from the line of Martin Parkhøi of Danske Bank. Please go ahead. Your line is open.

Martin Parkhøi

Analyst, Danske Bank A/S

Q

Yes, correct. Martin Parkhøi, Danske Bank. Just on China, you said that in the first quarter, I think that the growth has been low single-digit for the reasons that you have mentioned before, but [indiscernible] (00:27:12) guidance for the full year is 10%. What are the drivers behind the accelerating growth in the coming quarters? Is it just due to easier comps? And then, secondly, could you maybe elaborate a bit on the performance of Atos in the first quarter? And then finally, or as people tend to say, then secondly; the tax rate of 23% this year, what do you expect including Atos' tax rate will be on a more long-term level?

Kristian Villumsen

President & Chief Executive Officer, Coloplast A/S

A

Thank you, Martin. On your first question, on China; so we are basically [indiscernible] (00:28:06) thinking a double-digit growth here because of easier comps. But we are also expecting to see that there is going to be some level of uptake in how people spend money as we move through the year. We don't think that this is going to persist. We still see stable growth in new patients. And so, part of the effect that you've seen here in Q1 has also been some of the shutdowns that we've seen in large cities in China, but mainly a period of easier comps.

Second question, what was that, Martin?

Martin Parkhøi

Analyst, Danske Bank A/S

Q

The question was performance of Atos in the first quarter.

Kristian Villumsen

President & Chief Executive Officer, Coloplast A/S

A

So, Atos had a good year last year. They've grown double-digit. Their growth continues. And there is the drivers that we would expect to drive the growth. Provox Life continues strong performance. And we're also seeing solid contributions across the different regions. So, we feel good, Martin, about what we've said that you should look at this as a business that delivers in the 8% to 10% range. More to come once we close.

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

Yeah. And then it's me again, Anders; Martin, your last question around the tax rate. So as I said earlier, we are expecting that this year's tax rate is going to be around 23%, and that's also my expectation throughout the Strive25 period, including our Atos acquisition.

Martin Parkhøi

Analyst, Danske Bank A/S



Thank you.

Operator: Thank you. Our next question comes from the line of Veronika Dubajova of Goldman Sachs. Please go ahead. Your line is open.

Veronika Dubajova

Analyst, Goldman Sachs International



Yes. Hi. Good afternoon. Thank you for taking my questions. I have three, please, but I promise the third one's really quick. The first one is just on the price increases. And, Anders, I want to qualify a little bit or understand a bit your commentary. Because if I look at the organic guidance, it doesn't seem to have changed versus where you were a quarter ago when I don't think you were contemplating any price increases.

So I'm just trying to understand, are these on a group level, just not that material, which is why you're not changing the guidance; or are they being offset by softness from things like Omicron? Just, if you can help us actually understand the magnitude of the price increases that you've been able to take or kind of how much in terms of growth are these going to contribute to the fiscal year? And IU aside, are there any other products where you've been successful or categories? That's my first question.

My second question is just around the supply chain and we're hearing anecdotally obviously quite a lot around port delays, logistics issues, raw material sourcing. Just kind of curious how you feel about the supply chain as you have it, and how much contingency you've built in as we go through the remainder of the year should this persist? And then my last, I promise, a quick question is just remind us on your Russia exposure and whether you're seeing any changes there at the moment in terms of the demand, and any big tenders that we should be bearing in mind as you move into the remainder of fiscal year? Thanks so much.

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S



Yeah. So, thanks for your question. So, let me start around the price increases. Actually, I think we also called out when we announced our full year results that we are planning to do price increases across the business, and that's basically what we are working on. And we have already done some also here in the first quarter.

So, that is built into our growth guidance as well. I'm just saying that the part of the headwind we see across the raw material price increases are, you can say, passed on to our customers. But I'm not going to call out specifically how much, Veronika. But there is some of it that is passed on, but we're not able to pass on 100%, unfortunately, because a lot of our business is reimbursed.

In relation to your second question, our production and supply chain, that is still running. We are very satisfied with that. We have not been into very significant back orders. So, we are going – or we are supplying to the demand we see out there. But there is a lot of work going on, you can say, behind the scenes. So we are working a lot on making sure that we get the raw materials that we need in order to produce the volumes. But, overall, we are actually very satisfied with all the work we do across our production and supply chain units in order to make sure that we can supply to the demand we have. But there's quite a lot of work going on behind the scenes. I think that's fair to say.

Kristian Villumsen

President & Chief Executive Officer, Coloplast A/S

A

Yeah, you can definitely say that. Veronika, to your question on Russia; think of it as 1% or 2%. And I'd say, if your concern is how much it would impact us, we've been there I think plus-30 years and there's been some real ups and downs. So you can see that it could impact the growth profile of EM for a quarter or so, but not at group level.

Veronika Dubajova

Analyst, Goldman Sachs International

Q

Okay. That's great. And can I just clarify, Anders, the 67.5% gross margin guidance that you've given; presumably that's excluding Atos, just to confirm them.

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

That's what I see for the core businesses, Veronika. So I see it at that level.

Veronika Dubajova

Analyst, Goldman Sachs International

Q

Because my understanding was the Atos gross margin was higher than yours.

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

Yeah. So, the Atos gross margin is sitting around 80%-ish. So, what I'm still saying is that the combined companies will be around the 68%.

Veronika Dubajova

Analyst, Goldman Sachs International

Q

Okay. Okay. Thank you, guys.

Operator: Thank you. Our next question comes from the line of Maja Pataki of Kepler Cheuvreux. Please go ahead. Your line is open.

Maja Pataki

Analyst, Kepler Cheuvreux SA (Switzerland)

Q

Yes, good afternoon, and thank you for taking my question. I have two. I would like to start with China. Kristian, can you help us or can you tell us how you are thinking as Coloplast about China and the potential development of Omicron potentially leading to harsher lockdowns? Just, what is it that you have as a playbook for Coloplast in mind?

And the second question is, could you help us understand a bit about the growth profile of Atos? Has Atos suffered similarly to Coloplast's Chronic Care business due to lockdowns or infection rates spiking? Is there a general seasonality with revenues? Just to understand a bit more about how to think about a 12-month sales projection for Atos. Thank you very much.

Kristian Villumsen

President & Chief Executive Officer, Coloplast A/S

A

Thank you, Maja. So for China, I'd probably be a little careful predicting how Omicron is going to play out in China, as if I would know that. I can say we run a business in China where we have a very, very good feel for what the activity levels look like in the hospital setting. We run clearly the largest sales force that we have. We run the largest patient support program that we have anywhere in the world. So, we can see on a daily basis what the activity levels look like.

And we've seen the activity levels or the patient inflow numbers hold steady for quite a while. You've also heard us talk to that. And that the decline in the growth rate really has been about how much people spend when they basically buy from us. We're also very confident about our share in the hospital setting. We're very confident about the share in the consumer channel based on the data that we have.

We've seen the authorities be quite hard-nosed about on Omicron in a multiple settings here over the over the past few months. So, one city, Xi'an, in the northwest of China, 13 million people basically got a lockdown for a month. And what that means is then, of course, that as a company, the activity levels that you have of sending reps into hospitals doing in-field activities basically stops for a period of time. You're grounded. You can still serve the patients that you have in that area through your direct and digital channels, and we continue to do that.

We've also seen in Zhuhai, where we have our manufacturing, where some of the workers are basically not allowed to go to work because they're in a zone where you have lockdown. We can still maintain manufacturing and continue to supply. So, it is a bit of a dynamic situation, Maja. We are playing it dynamically, I would say.

But what gives me confidence is, one is the position in the market. we have a very large installed base of users, and we have a model which I think has been validated through the pandemic that it can work also. When times were really grim in the beginning of the pandemic, the model kept running, the company kept running. So, I think that can – that will still happen now. Of course, Omicron can have an impact that's bigger than what we can see right now. That's just the uncertainty that we're dealing with.

And then to your second question about Atos, there was some impact early on in the pandemic in Atos' performance on growth rate when it came to growth, but we've seen it actually be quite resilient. They've had a very strong year. And so, when we look at the business, it's double-digit growth in the laryngectomy business, and we expect that to be stable at that level, high single-digit, double-digit type of growth.

And then, for the tracheostomy business and I'll remind you that's more of a hospital business, we see growth in the mid-single digit growth range. We don't see big seasonality variations, because the type of demand that's underlying here is quite stable. It is quite stable. So, if you think of the robustness of demand and robustness of growth, it's high.

Maja Pataki

Analyst, Kepler Cheuvreux SA (Switzerland)

Q

Perfect. Thank you so much.

Operator: Thank you. Our next question comes from the line of Niels Leth of Carnegie. Please go ahead. Your line is open.

Niels Granholm-Leth

Analyst, Carnegie Investment Bank AB (Denmark)

Q

Thank you. Thank you very much. A few housekeeping questions. So, when you – how would you distribute the DKK 200 million of amortization between your individual cost lines, and would the full year amortization still amount to DKK 320 million? So, that was my first question. Thank you.

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

Yeah. Hi, Niels. It's Anders here. Yes. As I said earlier, we are expecting the full year amortization to be around the DKK 300 million. And for the eight months, we have included in our guidance, it's around DKK 200 million. And that will be one line in our P&L under the amortization.

Niels Granholm-Leth

Analyst, Carnegie Investment Bank AB (Denmark)

Q

But I guess you will have to allocate amortizations between your individual cost lines.

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

So, no, that's not something we are going to do in our full P&L. So, today, amortization is just one line. And I am expecting that will continue...

Niels Granholm-Leth

Analyst, Carnegie Investment Bank AB (Denmark)

Q

Excuse me. So, today you are allocating your amortizations since you are reporting based on functional items, your amortization are distributed between cost lines. So would the amortizations be included in – so, how much is in distribution cost, how much is in...

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

Ah, yeah, okay. That angle, that split I have not looked further into. And we are going to look further into that when we are announcing our Q2 result. If that's what you after, Niels.

Niels Granholm-Leth

Analyst, Carnegie Investment Bank AB (Denmark)

Q

Yeah. Yeah, sure. Okay, thank you. And then...

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

[indiscernible] (00:41:46)

Niels Granholm-Leth

Analyst, Carnegie Investment Bank AB (Denmark)

Q

It's okay. And further on the depreciations and amortizations, there was a decline of DKK 25 million or so in quarter one, which I suppose is related to the older acquisitions of Mentor and Comfort Medical where

amortizations are basically running out. So, is it fair to assume a positive effect of DKK 100 million or so from the phasing out of those amortizations this year?

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

Yeah. So, it's true. As you are saying, Niels, we're having a positive effect on the amortization in Q1, and I'm expecting for the full year that we will have a positive effect from this of around DKK 50 million. Please keep in mind, we also had a positive effect in Q3 and especially Q4 of last year. So it's not a full year impact that you can base your Q1 actuals on.

Niels Granholm-Leth

Analyst, Carnegie Investment Bank AB (Denmark)

Q

Okay. That's great. And then just finally, usually you give us a number for the net financials all together...

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

Yeah.

Niels Granholm-Leth

Analyst, Carnegie Investment Bank AB (Denmark)

Q

...for the full year. Would you be able to provide a similar number...

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

Yeah.

Niels Granholm-Leth

Analyst, Carnegie Investment Bank AB (Denmark)

Q

...for the full year?

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

Yeah. I actually called that out when I walked through with the various assumptions for the year, but we are expecting a negative financial income of DKK 350 million. So, minus DKK 350 million. And the way we look at it is around the minus DKK 200 million before the Atos and then around DKK 50 million for the financing. So that's one-off. And then around DKK 100 million related to interest cost for eight months. So, those are the underlying assumptions for the minus DKK 350 million that we are currently expecting at full year.

Niels Granholm-Leth

Analyst, Carnegie Investment Bank AB (Denmark)

Q

That's super helpful. Thank you so much.

Operator: Thank you. Our next question comes from the line of Yiwei Zhou of SEB. Please go ahead. Your line is open.

Yiwei Zhou

Analyst, SEB Enskilda (Denmark)

Q

Hi. Thank you for taking my question. And actually most of the questions have been answered. One remaining question [indiscernible] (00:44:13) question, the DKK 200 million amortization relating to Atos, Anders, could you please split it to – between the purchase price allocation and the CapEx into the R&D? Just want to get feeling of how much the Capex spending for Atos going forward?

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

Yeah. So, what you are referring to is that as part of the acquisition, we said that around DKK 200 million we will spend on integration. So we have not yet been totally specific on how much is going to the P&L and how much is going to the CapEx. But what I am still expecting that the majority of the DKK 200 million will be CapEx and especially related to IT, because we have earlier said that we will move the Atos Medical into the Coloplast IT infrastructure and that's where we are going to invest, and that will be a CapEx related cost.

Yiwei Zhou

Analyst, SEB Enskilda (Denmark)

Q

Sorry. My question is relating to the DKK 200 million amortization. Could you split it between the purchase price allocation and R&D CapEx?

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

That one, we're going to be a little bit more specific on when we are going to announce our second quarter results on how we're going to split it out. But as we said as part of the acquisition, it's around DKK 4 billion that we're going to amortize and it's going to be over a 15-year period. But the split, we're going to be more specific on in our second quarter results.

Yiwei Zhou

Analyst, SEB Enskilda (Denmark)

Q

Okay. Okay.

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

Sorry. Did that answer your question?

Yiwei Zhou

Analyst, SEB Enskilda (Denmark)

Q

Yes, yes, yes. Clear now. Just wait until Q2. My second question here is regarding the Urology business and seeing your financial note and just calculated EBIT margin of the Interventional Urology actually declined if you compare to Q1 last year. Could you elaborate a bit on this trend?

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

Yeah. So remember last year and we actually had a pretty strong start to our Urology business, but we were also in the middle of a lockdown. So the spending was not that high. So, we had global travel ban. Our Urology franchise did not spend a lot on sales and marketing, et cetera. So we started out with a pretty strong margin.

This year, we had a decent start to the year with around 5% growth, but the spending is significantly higher. So we are starting to travel again. We are having sales meetings. And we're also investing into growth and we're also investing into innovation especially related to our Nine Continents acquisition we did last – we acquired last year. So, that's why the margin compared to last year is a bit lower.

Yiwei Zhou

Analyst, SEB Enskilda (Denmark)

Okay. Very helpful. Thank you.

Q

Operator: Thank you. We currently have one further question left in the queue. [Operator Instructions] And the next person in the queue is Craig McDowell of JPMorgan. Please go ahead. Your line is open.

Craig McDowell

Analyst, JPMorgan Chase & Co.

Great. Good afternoon, everyone. Thanks for taking my question. Just one remaining for me and then a clarification. The first one, there's lots of headlines and data around nursing burnouts and shortages. And given that the nurses are important stakeholder in the distribution channel across your portfolio, I'm wondering, firstly, whether your sales reps have seen that in the ground? And if so, whether higher vacancies or higher turnover are having any impact on your businesses, or could potentially have a future impact?

Q

Kristian Villumsen

President & Chief Executive Officer, Coloplast A/S

So, a great question, Craig. The short version is, yes, we do see this. We do so this. We do see this both in Europe and the US, and then also in some markets in EM but more pronounced in the developed markets. And of course, to the extent that nursing shortages are so severe that they materially affect hospital activity, they could also impact our work. So, this is bad news for healthcare systems and also for anyone who works with nurses. As you can see in the sales figures for Europe, we have come through first quarter with something that looks like a more normalized growth level. So it's definitely one of the things that we keep our eyes on. We've gotten through, hopefully, hopefully the worst, but we still need to be mindful of it.

A

Craig McDowell

Analyst, JPMorgan Chase & Co.

And just to be clear, that's referring to the acute setting, but in the sort of community setting where your bulk of sales are, that's...

Q

Kristian Villumsen

President & Chief Executive Officer, Coloplast A/S

No.

A

Craig McDowell

Analyst, JPMorgan Chase & Co.

[indiscernible] (00:49:44).

Q

Kristian Villumsen

President & Chief Executive Officer, Coloplast A/S

A

No. It's way more pronounced in the acute setting. So if you think of the work that we do, Craig, for both the Continence Care, Ostomy Care, both of these businesses originate in the acute setting. And that's also where we have some exposure to nursing shortages. So we're monitoring it. We're still seeing the business I think perform better in Europe. And where we have the bulk of the headwind is really is in Continence Care in the US.

Craig McDowell

Analyst, JPMorgan Chase & Co.

Q

Okay. Understood. And then just a clarification, sorry, I might have misheard, Anders, earlier. But just to clarify, the gross margin commentary of around 68% at the lower end, that refers to the underlying business ex-Atos?

Anders Lonning-Skovgaard

Chief Financial Officer & Executive Vice President, Coloplast A/S

A

So, I also had that question earlier from Veronika. We are expecting for the combined to be around the 68%; and ex-Atos, in the lower end of the 68% based on the assumptions I talked through early on.

Craig McDowell

Analyst, JPMorgan Chase & Co.

Q

Okay. Thanks. I must have misheard. thank you.

Operator: Thank you. We've had a couple more questions come through. The next is a follow-up from Veronika Dubajova of Goldman Sachs. Please go ahead. Your line is open.

Veronika Dubajova

Analyst, Goldman Sachs International

Q

That was going to be my follow-up just to make sure I had not misunderstood you, Andres. So that's helpful. But maybe just a quick one on Wound Care. Quite an impressive quarter just looking at the Wound business, excluding Skin and Compeed. Anything kind of special you'd call out there, or is this continued share momentum that you're seeing on the back of the product launches? And maybe just related to that, refresh my memory, when do we see the silver hydrocolloid launch and maybe just a quick update on what the German market share looks like? Thank you, guys.

Kristian Villumsen

President & Chief Executive Officer, Coloplast A/S

A

Yeah. So, Veronika, Wound Care, great first quarter. And really driven by Europe and EM. And I'd say on the back of the fundamental commercial focus that we have around Silicone and Fiber. And we really have seen very strong work across markets in share gains. There is a little bit of one-time effect in Q1 where we've seen some distributors basically stock up, but there's still very strong underlying growth. When it comes to market share, you think about a community market share if you take just France and Germany, we are sitting around 10%. So, with the current growth rates compared to market, the company definitely continues to take share.

Veronika Dubajova

Analyst, Goldman Sachs International

Q

Sorry, Kristian, I was on mute. That's great. And can you quantify the stocking benefit? How meaningful was that?

Kristian Villumsen
President & Chief Executive Officer, Coloplast A/S

Off the top of my head, I can't. But it's a very strong growth quarter. So, the reason I called it out is that you are going to see – you're not going to see that same momentum continue into Q2. So, a bit of this demand that we saw here in Q1 could also have gone into Q2 under normal circumstances. And we also have a higher baseline in Q2, but it's still a strong underlying growth.

Veronika Dubajova
Analyst, Goldman Sachs International

Okay. That's great. Thanks.

Operator: Thank you. And we have one final question in the queue, that's from the line of Virendra Chauhan of AlphaValue. Please go ahead. Your line is open.

Virendra Singh Chauhan
Analyst, AlphaValue SA

Yeah. Thank you for taking my question. So a couple of questions. On the US GPO side, so are your US sales force able to go into the field and leverage your Ostomy GPO [indiscernible] (00:54:04) to the fullest extent now? And, secondly, does Atos have any presence in the GPO space for their products currently?

Kristian Villumsen
President & Chief Executive Officer, Coloplast A/S

So, thank you, Viren. So the US Ostomy business is a hospital contracts business. And with the opening of the GPO, I'll just say this as a reminder, the company now competes on an equal footing. But even with the opening, we haven't had full access because we basically see hospitals who don't want to see reps basically, right. So we can leverage some of this, but not to the full extent. So there's still some access limitations. We've also seen that here in this quarter.

We've gone ahead and still invested in the expansion of our Ostomy sales team and the expectation that these type of restrictions are going to diminish as we move through the year. We have a full Ostomy team – expanded Ostomy team now in place. So I'm expecting a good year, strong year for Ostomy in the US, and I'm expecting it to gradually accelerate as we move through the year.

Atos has good access in the US. I'll have to profess ignorance at this question. I don't know to what extent this is – the laryngectomy category is GPO driven. I can attest to that later on as we get to work with the company. But it has a very strong position in the US. And so when we think of the acquisition, of course, we think first, second, and third, we think about growth; and the US is very, very high on that list. But contrary to the legacy Coloplast business in Chronic Care, Atos has I think a more advantageous competitive position, in that there's not that much manufacturer competition for the business in laryngectomy in the US.

So I hope that answers your question.

Virendra Singh Chauhan
Analyst, AlphaValue SA

Yeah. Thank you, Kristian. That's helpful. Thank you.

Operator: Thank you. And as there are no further questions in the queue at this time, I'll hand back to our speakers for the closing comments.

Kristian Villumsen

President & Chief Executive Officer, Coloplast A/S

So thank you, everybody, for the interest in the company. And should you have any further questions or follow-up, please reach out to our Investor Relations team. I hope everybody is safe. Have a good day.

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