Q1 Trading Statement

Tuesday, 28th January 2020

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Operator: Ladies and gentlemen, thank you for standing by and welcome to the Greencore Group plc Q1 trading update conference call. At this time, all participants are in a listen-only mode. After the speaker presentation there will be a question-and-answer session. To ask a question during the session, you will need to press *1 on your telephone keypad. I must advise you that this conference is being recorded today on Tuesday, 28th January 2020. And I would now like turn the conference over to your first speaker today, Jack Gorman, Head of Investor Relations. Please go ahead, sir.

Welcome

Jack Gorman

Head of Investor Relations

Thank you, Yola, and welcome to everyone on the call this morning. My name is Jack Gorman and I'm Head of Investor Relations at Greencore. Thank you for taking the time to join us for our Q1 trading update conference call, which covers the period to 27th December 2019. I'm joined on the call today by our CEO, Patrick Coveney, and our CFO, Eoin Tonge. In a moment, I'll hand you over to Patrick to give an overview of trading in the period, and after that we will open up the call to Q&A. Finally, I would like to draw your attention to the forward-looking statements at the end of today's release.

Thank you, and with that I'll pass it over to Patrick.

Trading Overview

Patrick Coveney

Chief Executive Officer

Thanks, Jack. It's Patrick Coveney here. Let me reiterate Jack's welcome and thank you for joining us this morning. I'm joined for the call and the Q&A which will follow by our Group CFO, Eoin Tonge. This morning we released our Q1 trading statement for the 13 weeks to 27th December, as Jack referenced, and the purpose of this call is to provide some more colour to that trading statement and to enable Eoin and I to field any questions that you may have. We'd anticipate finishing at about 09.00.

When we last talked formally to you in late November at our FY19 results presentation, we were bringing our new strategy to life with customers, with investors, and we'd begun activating it with our acquisition of Freshtime. Consistent with that activity, the first quarter of FY20 has been all about continuing to execute further against our strategic and organisational objectives, notwithstanding the challenges and uncertainties that the UK economy and grocery sector experienced in that October-to-December period. We are happy with the progress that we've made in this regard and feel confident that this will be reflected in our commercial, operational and financial performance over the rest of this year.

This morning, I wanted to provide more colour on three topics: our Q1 revenue performance; our momentum commercially, operationally and organisationally during the quarter; and finally a reiteration of our FY20 financial outlook. I'll take each of these topics in turn, beginning with Q1 performance.

Q1 revenue performance

While seasonally quarter one is not the most important quarter for us from a trading and profit delivery perspective, we have made decent progress in the period. The overall market environment remained challenging and consumer demand was subdued, especially in October/November, so we were pleased to deliver modest growth against that backdrop.

To summarise and to be precise here, Q1 was very much as we expected it to be. Total revenue in quarter one was £367.8 million. Reported growth was 1.8%. Pro forma growth was 0.7%, adjusting for the impacts of Freshtime and also for the revenue from site exits last year. This represents a modest improvement in the overall rate of growth that we achieved in the second half of FY19.

Breaking down this pro forma growth, food-to-go categories grew by 0.5%, and growth in other convenience categories was 0.9%. Our performance in the food-to-go categories during quarter one was delivered against a subdued and uncertain consumer environment, and also, importantly, against a comparative period last year where we delivered 6.4% growth. The overall market environment, while subdued, has stabilised now after the decline that occurred in the second half of 2019. IRI data for food-to-go sandwich, salad and sushi indicates that the market grew by 0.1% – flat, in effect – in the quarter to December, and we delivered a little ahead of that level of market growth.

Encouragingly, year-on-year growth improved through the quarter, with both the market and ourselves delivering a decent December and good Christmas trade. We continue to see a greater level of variance than typical in trading performance across our customer base, a feature that has now been evident for a number of trading periods, and whilst not in the pro forma comparison we do want to note that Freshtime performed well in the quarter on all metrics, at least in line with the expectations we had at the point at which we acquired the business.

In other convenience categories, pro forma growth was 0.9%, back into positive territory after a modest decline in the second half of 2019. This growth was driven by the ready meals business, which has continued to build on the improvements achieved in half two of last year. This positive ready meals momentum was in part offset by lower Irish ingredients volumes in the period.

Momentum

Our momentum commercially, operationally and organisationally has been good during the period. In commercial terms, we've made good progress in the quarter, with several successful launches in sandwiches and ready meals that provide us with good performance momentum as we look into the rest of the year. The pipeline of commercial activity is also healthy. We have many initiatives under way with customers to activate volume growth plans for the seasonally important second half of our fiscal year.

Alongside broadening our product proposition, we continue to develop supply chain, waste and availability initiatives, in all case jointly with customers, to enable consumers to buy more and to enable our customers to sell more.

And people often ask about how we match our launch activity to the relevant key consumer trends of the day. In this regard, I thought we would cite one example, which is the role that vegan and vegetarian products are playing in our new product introductions. And if I take the 77 new seasonal sandwich SKUs that we would have launched, which are effectively what would be loosely described as 'Christmas ranges', 22 of those 77 SKUs were either vegan or vegetarian.

Our operational excellence programme remains on track, and we are delivering against internal expectations there. As we noted in November, the focus of this year is to use these programmes to defend or enhance margin, to drive improved operational performance and to build consistency across the group.

The pilot projects on automation are proceeding really well, and we're excited about the types of return that could be on offer from strategic capital investment in these areas, spanning both our food-to-go and ready meal sites. Importantly, these excellent programmes provide us with useful levers to mitigate against ongoing labour inflation. Separately, we note the emergence of some specific raw material inflationary pressures, especially in pork-related products, and we are recovering this principally through price.

Turning now to just organisational changes. As referred to earlier, we continue the integration momentum around Freshtime, and this has proceeded really well on the quarter, with more to go as the year progresses. In December, we installed a revised and new senior leadership structure that will allow us to better balance business ownership with autonomy and entrepreneurship, and also to balance that against the well-progressed functional excellence agenda that I described a second ago. Central to this was the establishment of five separate business units, with the directors of those units now sitting on my broader leadership team.

FY20 financial outlook

And now let me bring all this together with a reiteration of our FY20 outlook that we first communicated to you in late November. We are anticipating another year of profitable growth in FY20. As we outlined in November, we anticipate that revenue and profit growth will be weighted towards the second half of the year, as is typical with Greencore. Alongside this, we continue to anticipate strong free cash generation and conversion and solid group returns.

Conclusion

Let me now conclude with some final remarks, firstly just to remind at least some of you on the call that we will be hosting our AGM in Dublin later this morning and we look forward to seeing some of you here. Secondly, I wanted to draw your attention to a separate RNS that we released earlier this morning. We have announced two new non-executive director appointments. Helen Weir, who is a former CFO at Marks and Spencer and John Lewis and has deep knowledge of the consumer sector, will join the Board effective from 1st February. And Paul Drechsler, who is a board member of the International Chamber of Commerce, has previously served as president of the CBI, and has deep and wide executive and non-executive director experience, will join our Board effective from 1st May.

Helen and Paul will join Gordon Hardie as new members of our Board. The appointment of Gordon was announced in December and becomes effective from 1st February. He brings 30 years of expertise from his career in the global food and FMCG industries. These individual skills, as well as the extensive experience and expertise, will be highly beneficial to both the Group and to our Board.

And finally, let me just remind everyone that our next results statement will be our interim results on 19th May. So thank you for listening to me; hopefully that gives you a little more colour around what's driven our business in the first half and how we're thinking about the rest of the year. With that, Eoin and I are happy to take some questions.

Q&A

Operator: As a reminder, to ask a question, please press * and 1 on your telephone keypad and wait for your name to be announced. To cancel your request, please press the # key. Once again, to ask a question, please press *1 on your telephone keypad.

Your first question comes from the line of Darren Shirley from Shore Capital. Please ask your question.

Clive Black (Shore Capital): Morning, gentlemen. It's the shorter, wider one: Clive Black. Could I just ask, firstly, have you seen any evidence of a change in mood from your customer base, or indeed the consumer, since the UK election in mid-December? And secondly, can you give any more colour around what you call the pipeline of activity, Patrick, with respect to Greencore's developments in forthcoming quarters?

Patrick Coveney: Yes. I mean, Clive, I want to be – I want to be careful in not – in not overstating this, and you'll have heard me reference it in my talking points. So we saw the convenience food market, and within that most particularly the food-to-go market, step back into growth in December from the more flat performance that we saw in October and November. I think there is some anecdotal evidence that that's reflective of a bit more consumer certainty, a bit more consumer confidence. As you well know, I don't think our customers knocked the lights out in terms of Christmas trading, but it was solid enough. And we began to see that in, you know, both the IRI data as it relates to our product categories and our performance against that.

So we do feel a little bit better about December then we did in – about October/November in terms of where consumers are and what that means for the performance of our markets and our performance within those markets. And, broadly, that's continued into January. But, you know, let's see how the second quarter unfolds as we go forward. But we – my judgement is that there's just a little – there's certainly less uncertainty, and there's just a little bit more confidence and positive sentiment in the market than there was before the election. That would be my judgement, but let's see how they – how the periods unfold.

I mean, in terms of initiatives, I mean, we are very conscious of the metrics and, more importantly, the strategy that we have around delivering sustained mid-single-digit revenue and volume growth in our business. And we don't make those – that comment lightly, and we know it needs to be backed up with the commercial activity that we've got across the different categories, and we feel we're in nice shape there in terms of the relaunch activity, and rearranging activity in a number of core categories with core customers. Some of that happened in December and is – and is now rolling into Q2, some of it will happen at the back end of this quarter, some of it will come to market in in Q3. And we're also – we're quite pleased with the level of recovery that I referenced, both in terms of volume revenue and consumer sentiment around the ready meal part of our business, and we think that will give us progressively stronger momentum as we go through the year. So – and, as you'd expect, we – you know, we continue to hunt around for opportunities at the edge of our traditional, you know, grocery multiple customer set. And I think, again, we would hope to add to all of that in those areas. So that will be a little more generic than I expect you wanted us to be, but the kind of big point here that I want everyone on the call to know is that we feel we've got a nice pipeline of commercial initiatives here that is consistent with where we need the business to be in terms of growth as we look forward.

Clive Black: That's helpful, Patrick. Thank you.

Operator: Your next question comes from the line of Ned Hammond from Berenberg. Please ask your question.

Ned Hammond (Berenberg): Hi, good morning. I have a few questions, please. The first one is on the stat that you gave on vegan and vegetarian products. Is that reflective of the overall proportion of NPD that is vegan-related products at the moment? Secondly, is there any change to your cost inflation expectations as a result of the national living wage increasing by slightly more this year? And then, lastly, I was just wondering if you could provide an update on what proportion of your employees are EU nationals and also what proportion of new hires are EU nationals.

Patrick Coveney: Hi, it's Patrick. Let me take the first question. and Eoin will provide the update on inflation and the shape of our employee base and how that's evolving as we look through this year. So, I mean, the – probably the easiest way for me to just describe the role of vegan/vegetarian/meat-free products is just to describe the – our SKU base last year and how that's shaped. So, very roughly, we had 2,500 SKUs in the market last year, of which 1,200 – in other words, almost 50% – were actually introduced in 2019 itself. Some of those were very modest changes to previous products. Some of them were fundamentally new ranges.

Of those 1,200 new products, 300 were either vegan, meat-free or vegetarian. So that represented more than – actually more than a quarter of the total new introductions, a bit more than 300. So that's a – that is probably a trebling of the products in those areas relative to 2017 or 2018, so a big step up. Now, I would also say that that percentage of new product introductions would not be mirrored in the percentage of overall revenue. So there's a lot of new activity in this space. Not all of it is cutting through successfully to consumers, but it's certainly indicative of very strong desire from consumers and also from our customer set to have lots of convenience food product areas that meet those needs. And our plans for '20 would be broadly similar to 2019 in terms of the relative contribution of products of that type.

Eoin, do you want to pick up the other two questions?

Eoin Tonge: Yeah, sure. Ned, morning. So I think, in terms of national living wage, yes, it was a little bit ahead of what we would have planned for – I think what everyone would have planned for. But I think the overall message is similar to what we would have said at the end of last year: that we expect labour inflation to be circa 5% again this year, so not a material change to our budget assumptions around labour and recovering that labour inflation through both our cost efficiency and also through our various different innovation initiatives that Patrick referred to.

In terms of the split of our workforce, I mean, broadly we have about 45% EU nationals in our – in our workforce. That's been stable enough, actually, in the last couple of years or so, actually. I don't exactly have to hand that – the exact split of our new hires, but we don't believe the picture has changed that dramatically.

Ned Hammond: Okay, great. Thank you. And just a final one on that – on the national living wage side of things, just looking out a bit further into the distance. Do you pay your – all of your staff the national living wage, regardless of when they're 25, or is that something you'll need to move to?

Patrick Coveney: Yeah, yes. We do. So that's something we did almost from the off.

Ned Hammond: Great, thank you.

Operator: Your next question comes from the line of Sarah Stokes from Goodbody. Please ask your question.

Sarah Stokes (Goodbody): Hi, guys. Just two questions for me. Just – in previous statements, you've mentioned the mix performance within your retail customers. Is that something that you're still seeing on the ground? And if you could just touch on cooking sauces: that would have been a challenging comp during the last period. How is that business shaping up for you now?

Patrick Coveney: Yeah. Two things. I mean, the – this trend in – and it's most particularly in sandwiches around quite a high level of variation in volume and revenue performance across our customer set – that has continued in Q1. And the reason that it's a little different from what we might have seen in prior periods is we're seeing some customers up close to double digits, other customers down close to double digits. But that's happening without there being any changes in our market share or market position, either up or down in that case, so that's – that's why we're kind of pointing it out as been a little different.

And I think it creates, you know, clearly opportunities for us to continue to run very hard with the guys who are trading above market, but also I think it gives us a real agenda on product, on availability, on supply chain initiatives to tackle people who are – who may have lost some footfall more than they should in that particular space. So the – and we highlight that because certainly, if I reflect on the last ten, 12 years of doing this job, really in the last 18 months we've seen – we've just been more struck by that level of variation in customer volume performance period on period, and – and that's what we're highlighting.

Yeah, cooking sauces. I mean, we had – just to kind of demystify it a little bit, Sarah. I mean, we had challenges in the second half of '18 and into '19 in terms of delivery in our Selby cooking sauce business. We'd grown very strongly, and we couldn't quite keep capacity up with demand. And that led to us – that put some real pressures on us in terms of service and, as a result, through in terms of combination of customer confidence and ultimately financial delivery. I think the journey we've been on since the second half of calendar year '19 has been pretty good in that regard. We've got a lot more stability there now. We're back at the right kind of stock levels that you need to be for a make-to-stock business like that. We've got a team that are really delivering in line with the plan that we need for them.

I think that may take – that may take a number of periods for that to begin to take the financial performance where we'd ultimately want it to be, but in terms of the stability of the site commercially and operationally, it's where we would – where we needed it to be, and I think we're pretty pleased with where we are.

Eoin Tonge: And, from a revenue perspective, it was pretty much stand on really in the period.

Sarah Stokes: That's brilliant. Thank you, guys.

Operator: Once again to ask a question, please press *1. Your next question comes from the line of Roland French from Davy.

Roland French (Davy): Right, morning, everybody. I've got three questions. So, I guess, firstly, on profit phasing, I know you've mentioned the back-end weighting as regards growth, and I know there's a typical seasonality to profits. But just given the growth split and the weighting in H2, I guess taking into account your comments on raw material – I know there's been – there's been more volatility in raw material base generally, how should we think about the underlying profit performance or growth in H1 year on year? That's the first question.

And then, I guess, second, could you maybe just give us a little bit more colour or granularity on the performance of the food-to-go adjacencies? So that's salad, sushi, and I know there's some trials in hot food and snacking. Absolute growth rates – is the growth, you know, primarily velocity. or is there – is there some new distribution wins within that?

And then, thirdly, aside from a consumer rebound, what do you think could lift the market growth rate? So the market growth rate has been flat for a couple of months. I know you said December has picked up a little bit, but what do you think could lift that growth rate to 1% to 2%?

Patrick Coveney: Eoin, do you want to deal with the profit phasing and I'll pick up the other two?

Eoin Tonge: Yeah, I mean, Roland, morning. I think, as you say, typically we are a second-half-weighted business in terms of profit delivery. So it's typically really about a 40/60 split. Freshtime adds to that a little bit. And I think, as you say, as the way the year is building, given from a revenue perspective, our expectation is that it builds through the year, through a combination of both the initiatives Patrick referenced, but also to do with the relatively softer comps in the second half of last financial year. The inflation and inflation recovery is a little bit volatile, and that will – might have a bit of an impact on the phasing, but we do think the phasing will be maybe a little bit more than last year, but in and around that 40 to 60% split.

Patrick Coveney: Yeah, Roland, if I just pick up on food-to-go adjacency, I mean, the kind of simplest way of putting it is where – we're where we want to be across each of those areas. The most material is salads, where, you know, we've not only, I think, done a nice job of organisationally and operationally integrating Freshtime into our Group, we've also got some revenue momentum there where the increase – the capabilities that have come with Freshtime we've been able to deploy into other Greencore customers. Some of that will be part of the commercial pipeline that will feed through in the – in the second half of this year.

Sushi – the big – the big change we had there was bringing real raw fish or fresh sushi to market in the second half of calendar year '19. That's trading nicely for us, and consumers like it. And it's, you know, brought the real quality credentials to the prepacked sushi in the customers in which it's in, which I think is helpful. And we're in an early enough phase of chilled snacking, but we've got lots of product in development. Some of that is actually coming out of the original Freshtime site in Boston. And probably in terms of – in terms of organisational focus, hot food is probably getting a disproportionate amount of that, with trials either in the market or in planning across most of our customers to try to bring hot food offerings, particularly around breakfast, with some kind of sandwich-type product into market over the next while. So, you know, we cited those four thematic areas because we felt they were important alongside the traditional chilled sandwich business, and we're pushing hard against all four.

In terms of your final question on, you know, what's going to deliver growth, I mean, you know, what we can control and influence is our own portfolio, our own customer set. And what we've got is a set of product and activation initiatives that are rolling out across those. So we think that's going to get us to where we need to be in terms of the – you know, the revenue and volume outcomes that are implicit in the comments that we've been making this morning, which is that I think we have a – we've got a sense of conviction and confidence that you're going to see a level of growth build in our business through the rest of this year. And so that's where that – that's what we're doing.

And sorry, you – just to finish, you referred to or picked up on my point around the last four weeks being stronger than the first eight or first nine weeks of the quarter, and again, that's true. Whether you can attribute all of that to just a little bit more confidence and certainty in the UK than before the election, I'm not sure, but, but certainly arithmetically we're seeing that.

Roland French: Okay, that's good. Thanks

Operator: So your next question comes from the line of Damian McNeela from Numis.

Damian McNeela (Numis): Hi, good morning, gents. A few from me, please. Just on your comments about the customer performances, is there anything else you can sort of provide in terms of whether the performance is regional, sort of ex-London, or whether it's anything to do with the store estate of any particular customer? Just sort of wondering if you can make any comments there, please.

Secondly, on the CAPEX, you're talking about investing in automation, which you flagged before. Can you just remind me what is in the guidance for this year in terms of CAPEX and whether that includes the investment in automation? I know I should know that, but apologies. And then, finally, the third party: can you give what proportion of revenues were third party distribution, please, as well in the quarter?

Patrick Coveney: Hey, Damian. I'm going to cover the second and – sorry, the first and third, and I'll let Eoin pick up the points on CAPEX guidance. First of all, on third party, there's no material change in the – in the proportion of revenue that's third party, yeah, aside from the modest tweak downwards because of Freshtime [inaudible] –

Damian McNeela: Yes. Yeah, yeah, yeah.

Patrick Coveney: But broadly it's about sort of 7 to 10%, probably closer to 8% of our food-to-go revenues would be third party, or factored goods as we would call it. And, as I've said many times, the rationale for us doing that is because – is because we already have a – what I've described as sort of a pipe into small stores for sandwich product, and we're putting – we're putting complementary chilled products alongside that. But there's been no material change in that apart from the downward tick in the relative percentage because of the Freshtime business.

On what's kind of driving difference in customer performance, I mean, you –I'm going to be – to be very cautious and, indeed, fair in terms of how I describe that, because of the fact that we're working with all customers to try to drive their performance. But the points I would say is that it's not regional. As we look at our customer mix, we're – in other words, we're not seeing differences that can be explained by the regional location of stores. I think it is undoubtedly influenced by the quality of the – and investment in and appropriateness of the store estate. And I think, you know, retailing and store standards and morale within some of those stores is also a contributing factor. But they would be the things I'd say.

Eoin Tonge: Yeah, just on the CAPEX question, I'll help you out. The first thing I'd say is that our guidance on the maintenance CAPEX is – it stays about – it stays the same, roughly 2% of total revenue. And in terms of total CAPEX, we had, as you remember, circa £43 million last year. I did guide at the end of last year that I did expect it to be higher through a combination of the automation and also growth initiatives. So the level to which that – how much higher that is just dependent on delivery of some of those projects in the financial year, and we'll be guiding as we go through the year in terms of how that looks. But certainly, as it stands now, it's definitely going to be in and around the 50 million range.

Damian McNeela: Right. Okay, that's brilliant. Thank you very much, Eoin.

Operator: We have –

Patrick Coveney: Great. Guys, listen, we said we were going to finish off by – at about 09.00. So we've just ticked past that, so thank you to everyone for joining us. If there are any incremental questions, I'd encourage you to follow up with Jack, who'll be around over the course of the day, but Eoin and I are going to need to head off to get ourselves ready for the AGM. So thanks for joining us, and we look forward to talking to you all in May. Bye-bye.

Operator: That does conclude our conference for today. Thank you for participating. You may all disconnect.

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