



Vinda International Holdings Limited
2019 Q3 Results Conference Call
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Speakers

Mr. Christoph Michalski, CEO **(CM)**
Ms. Vicky Tan, CFO & Company Secretary **(VT)**
Ms. Josephine Wong, Senior Corporate Affairs Manager **(JW)**

Presentation

JW: Good Morning ladies and gentlemen, welcome to Vinda International's 2019 third quarter results briefing call. I am Josephine Wong, Senior Corporate Affairs Manager. On the line we also have our CEO, Mr. Christoph Michalski, and CFO, Ms. Vicky Tan. Today's call will last for about 30 minutes. Christoph will first present the results and then we will open for Q&A. Just a reminder, we have sent you the presentation decks this morning. Please check your email box or download it from our website if you missed it. Now I'll pass the time to Christoph. Christoph please.

CM: Thank you. Good morning everyone. Thank you for taking the time to join us this morning. Before we start with the results, let's talk a little bit about the environment. You're probably very well aware that GDP was published for China at 6%, which is very much lower than most of people probably have expected and also slowest pace since 1992. There's a decrease in PPI index gradually over the last 4 months, and also the currency pattern, CNY vs USD; it's basically slowly declining again against US. So that's a little bit on the Chinese outlook - what we see. When we look at Hong Kong, clearly we do not know when the social unrest in Hong Kong will come to basically stop, and we'll see a very significant decline in visitors, and we start to see also decline in the retail sales in Hong Kong overall. Third point I would like to make is on pulp prices, we are now at all time low for both long and short fiber. We see some decrease in the warehousing and support in China, but not very fast. And we expect our prices to stay up to low level to the end of the year. And then basically, as you know, I'm not very good at forecasting the pulp price, but probably the next step would be increase. But we don't know how steep and when.

When you look at our Q3 results, we think they are very much in line with our previous performance. When it comes to growth, it's grown up 14.6%, which takes the overall growth year on year at 13.6%. Gross margin has improved not just because of our improved pulp, also a little bit of mixed effect involved, which is very good. And then, this additional gross margin

of 4.2 points year on year, basically lead to improve the operating profits, stands now at 9.6%, in an improvement of 5.9 points to last year, and EBITDA margin of 16.8%.

All these numbers in Q3 clearly had positive effect over year on year performance, and again gross margin now stands at 29.2%, operating margin 8.5% and EBITDA margin at 15.6%. So overall we think this performance is driven, as I said by growth, but also by the lowering pulp prices and some mix elements, and we are quite pleased with those results.

When it comes to Q4, I think we see there's a trend, a little bit under threat when it comes to growth, we expect our growth maybe to be a little bit lower and that had to do with starting of seeing lower prices and tissue market in China, which either we will have to basic to counter with some additional promotion or selective price decreases, but very selectively, so we will not do that across the board. And the other thing with Q4 is basically due to exchange rate which depending on the trade talks between US and China. Overall, I think for the year, we see solid results coming up, so Q4 will not be spoiler, probably will be in line with previous quarters, with these two risks that I just mentioned.

Good, I think you have got the deck. You probably have already read it. As you know, it's Q3 results, we only give you a very top-level P&L, it's not much for me to add in this presentation. So why don't I open for questions.

Q&A Section

Anson Chan (AC) from Daiwa Capital Markets

AC: Very good results - I have two questions. The first one is about tissues. What is the breakdown in terms of volume mix and price factors in terms of the growth, in particular, in China? The second question is on the personal care business – the announcement mentions that there's a slight recovery with good momentum – how should we look at the sustainability of that momentum? What has been done behind that?

CM: Thank you. When it comes to tissue growth in China, we have a slight sign of higher growth in value and in volume but they are not miles away. As we said, the success of Tempo and 4D-Deco continue to grow faster than the rest of our portfolio. Tempo and 4D-Deco together are around 20% of our sales and that always gives us a slight positive mixed effect. When it comes to price, Q3 over Q3 last year, there is no price effect. You remember we increased the price in Q1 & Q2 in 2018, so the price effect is gone. I think when you look at pricing for Q2 over Q3, there is only a very slight effect because we basically tried to delay any price changes as quickly as we can.

When it comes to personal care, I think the recovery that we are seeing is totally sustainable. Because we had a recovery in south-east Asia on baby, which was very good. So we implemented Oracle at the beginning of the year which had some operational challenges and the market was quite competitive. We have now moved to Oracle, that's all done, we have put a slightly new commercial policy in place, which is paying off.

When it comes to China, the effect of personal care is a little bit hidden. It's actually doing very well, when it comes to feminine. As I said to you, we had a relaunch in June, which resulted in July, August and September in quite significant listing fees and listing rebates and things like that. So, the sales momentum in volume is very strong. And the sales momentum in value is a little bit held back by the listing fees.

But overall, if we can judge after 3 months, we are quite pleased. As I said, it always takes 9 months to a year to really understand the consumer response and how sustainable your business is with a new brand launch. For the moment, we still remain very confident.

Dina Yat (DY) from HSBC

DY: Hi Management, congratulations, very strong 3Q result. I have some questions, so first is regarding your premium products under Tissue. Christoph, you just mentioned that Tempo and Déco contributed 20% of total tissue sales, can you remind us what was the contribution last year 9 months 2018, thank you.

CM: Premium products basically we didn't do analysis because it's too hard for us to see on the growth margin evolution what is pulp what is mix, etc. So, when it comes to last year, clearly this contribution was much lower, we don't really report these numbers every quarter. To give you an idea, it's about 20% now, and last year I think it was probably around 15%; a little bit lower than 15%. I think the key point I would like to make is that even in front of the market which now goes into the price increase and additional competition, I think our portfolio is much stronger than it has been 2016, 2017 before the pulp price actually increased that dramatically. And as you remember, in 2018 when we started our price increases at the end of 2017 beginning of 2018, we were actually able to do that. There was good momentum of the second price increase which slowed the momentum down but kept margin in a reasonable way. And I think now it's not surprised the decrease price of overall market; I think we are very well situated to defend the price decrease and to slow that down. Also, just for your information, we haven't reached from our production prospective, the bottom of the pulp price, so the bottom I think within the market and purchase. But, as you know, we have four months' lag of purchase to production, and therefore we still have in Q3 higher pulp prices that we would have in Q4.

DY: Ok, so for the last point you mentioned, you would expect your GPM to continue climbing up in 4Q, despite the price cut or you expect that to counter the potential price cut in 4Q. And if you could kindly share like what kind of magnitude of price impact would likely to see in 4Q or the level of promotion. Thank you very much.

CM: I think we should be some positive effects on gross margin in Q4, it might not be as significant as we hoped based on the comment you just made. You're right - but we have to increase promotion, or we have to take some pricing action at some stage. But, as I said, I think the portfolio is much stronger now to counter that. I cannot really give you a number because you know these are decisional months, as you know we have Double-11 coming up, which is an annual competitive month or competitive days. Also, we have Chinese New Year much earlier so probably there will be some sales to cover Chinese New Year and December, so still very hard to judge. But I think what we can assume is that Q4 will be a very good quarter again. And we should have very good numbers at the end of the year.

DY: Ok, may I ask one more question? Or two more questions?

CM: Sure, please.

DY: Ok, thank you. As you mentioned about Double-11, things on e-commerce also change quite fast. And I believe you're adopting very well in the past. But after you have achieved so many years of strong growth on e-commerce, do you expect a similar high growth during double-11,

or you would more focus on your profitability online? Or you do not have a very aggressive sales growth target during the major e-commerce event.

CM: So, when it comes to last year, we had an exceptionally good Double-11 as you might remember. And Double-11 was I think a little bit less successful seen by the industry because it has already peaked quite a lot. So, my expectation is that Double-11 would probably be a little bit less strong than it was last year when it comes to growth. But my expectation is that we would lead the pack in doing a very good job in terms of market share compared to our competitors. Our strategy has been since 2000, I think we changed a bit in 2017, to clearly, we have always one view on the growth which is clearly very important. And we also have the view on the profitability to intense e-commerce to use some of the higher margin SKUs in order not to basically go too negatively or not to lose too much margin in Double-11, but clearly it's an exceptional event which is more a volume driver than probability driver. When we look at the overall e-commerce development for the year and for the quarter it was very good, you see the slide on the last page, when coming back to China e-commerce sales are basically 35%. And I think it would below 30% about a year ago, it's going very fast. But actually, all channels on the year today prospective are performing better than last year. We have positive growth in distributor which was under stress last year, key account that we covered well, B2B is continued to grow, and e-commerce again is in a very high growth way. So, we're overall - the portfolio is getting a bit more balanced, when it comes to performance, and we are very confident that we can maintain our position.

DY: Ok, thank you. And my last question is also going back a little bit to the demand side. Your premium products have been growing quite well. So, I want to understand would you have any impact on your growth by city tiers? Was the growth in premium products driven by Tier 1, Tier 2, or wealthy regions? Or is it pretty much alike across the board? Thank you, that's my last question.

CM: I think - here's the answer very quickly. Our premium ranges are growing well cross the board, in particular urban areas. You always find across China, part of the population where, at least when it comes to the Vinda brand, of 4D-Deco – they are very attracted to that. For Tempo our distribution is a little bit more restrained when it comes to offline but clearly national when it comes to online, and probably Tempo is more Tier 1, Tier 2 and Tier 3. But I think the overall premiumization of the market is despite the relatively slow down of the GDP, still not changed at all. So, we do not see a significant change from that perspective.

VT: And also due to we invest all our AMP and promotion mainly focus on this premium category.

CM: Yeah, that's a good point Vicky, thank you.

Nicolas Wang (NW) from Haitong

NW: Congratulations management for the very extraordinary results. Just a couple of questions. Firstly, about the competition. I noticed that competition in the retail front is rather intense in mainland China nowadays. So I want to say that you mentioned that today you will reduce the prices of certain product lines. Could you give us more specific product lines which you are going to reduce price to increase competition?

CM: Not really – because that’s clearly quite a competitive thing. But what I can say is probably more how we manage that rather than what it is. So what do we do we always set price essentially in China and we definitely set a normal selling price and promotional minimum price. And these prices are then used region by region depending on their competitive environment. And clearly it works in the market they only use it if you really have to. Because you might remember when we took the prices up we took them up across the board. One of our competitors took them up a bit more selectively and that was probably the smarter approach. And we have decided also now in the price pressure for a downturn to be very selective and really follow a more differentiated approach. So that is probably the only thing I can really say about pricing.

NW: Okay. Thank you! Second question is about the margin. I noticed that the OP margin expansion in third quarter is higher than your gross margin expansion. So could you give us some colors how you managed that? I remember you have a plan for sanitary napkins launched of this new product at the end increase market penetration in the second half. That's number one. Number two, as we discussed before, you consider not price cut but doing more branding and promotions for your products. So how can you match the operating expenses as a percentage of revenue decrease?

CM: Well there are two effects. I think that the price high in pulp, we have changed our culture a bit and we all know perpetual term of pulp and sales and marketing or G&A either are basically very rigorously scanned across the board on a very regular basis. The second thing is with the growth we achieved a higher level of scale. And so I just to remind you when you look at generally speaking number of employees that has normally grown quite in line with our business growth up to 2016&17 and since 2017 the overall number of employees of Vinda has been changed by the company is now 20 percent or so larger. So we get a scale effect and we are a very cost conscious and therefore independent of the tissue of the pulp price movements. We try to run a very tight ship. When it comes to the investments in feminine care. You know there are two things. I mean Vinda has achieved our size of quick and modest but when we have this type of launch clearly our negative expenditure on feminine. We're not told to destroy Vinda's margin. So I think that is good news that allows us to have a little bit off of long term view on these investments. And I think why the negatives that did allow us to improve our margin especially when you have such a strong gross margin effects over the year.

NW: Okay! I understand. The last question is about the sales mix. On slide 3, it said the personal care sales contribution already declined by 2 percentage points, so that means

that the tissue business is going much better than the personal care. Are you introducing more personal care products in the mainland China market? When we should expect that the personal care business to catch up?

CM: No, I think you would have asked me four years ago when I was the sales contribution be in four years later. I would have never guessed that our percentage of tissue would further increase and this is not because of a bad performance of personal care. This is because our tissue performance has been so good. Our personal care portfolio, as you know tends to be a little bit more outside than inside China and these markets don't have the same market growth like Malaysia and Singapore and Taiwan and Korea and some of the export markets in Southeast Asia which are a little bit smaller. So what you see here is in effect China we have slowed down a little bit of expansion during the maximum pulp price in 2017 & 2018. Now we are starting back as I mentioned in H1 results call. And basically, I expect this over time to invert in terms of trends.

But clearly the last thing we will do is to slow down our expansion in tissue and therefore personal care will always compete very strongly with a very strong growing tissue business.

NW: Which is the main channel for your tissue? I mean the Personal Care business in China nowadays. So are you going to promote much of the Double 11 festival comes?

CM: Yeah I think personal care generally speaking it's about the majority of sales are in e-commerce and that is because you get a very clear basically coverage of distribution. And then we have for the feminine role of taking a very specific price region by region approach and that my expectation is that the e-commerce channel will dominate our personal care sales in China. Secondly when it comes to Double-11, I think the experience that we have had with Double-11 that was incredibly good for very well-known brands and you see top five brands who would basically make the majority of the business because of brand awareness and consumer understanding of what they're buying. So I think Double-11 is not particularly an opportunity for a significant brand launch. You might remember when we launched 4D-Deco we launched it first exclusively with one of the e-commerce platforms and that was outside the double-11 friendly but basically an enormous type of thing. And then you get very good responses because the overall noise level is not strong. So don't see Double-11 is a very significant driver for our feminine launch. But real focus maybe on Tempo and Vinda brand.

NW: Okay fair enough. Thank you very much Chris.

CM: Yeah you're welcome. Okay. Good. Seems to me there's no question left. Thank you very much for your time joining the call this morning. And I'm very much looking forward to seeing you and meeting you in person in January, actually in February after the Chinese New Year because Chinese New Year is so early this year. And until then I wish you all the best of success. Thank you.