PZ Cussons Q3 Trading Update

Wednesday, April 24, 2024

Operator Hello, all, and welcome to the PZ Cussons Q3 trading update. My name is Harry and I'll be your operator today. If you'd like to ask a question, please dial star one on your telephone keypad to enter the queue. It's now my pleasure to hand you over to Jonathan Myers to begin. Please, go ahead when you're ready.

Jonathan Myers Thank you, Harry, and good morning, everyone. Thank you for joining Sarah and me on the PZ Cussons Q3 trading update call this morning. By now, you should all have seen this morning's announcement, so I'll touch briefly on current trading and other developments in Q3, and then provide a little more colour on our announcement regarding plans to maximise shareholder value through portfolio transformation following a strategic review of brands and geographies. Sarah and I will then be happy to take your questions.

Before going into the detail, I'll just start with three key messages. First of all, trading is on track with improved volume-driven momentum in our business in Q3. Secondly, with better access to dollars in Nigeria, our balance sheet has improved, and we have good visibility in terms of our ability to make further significant progress over the coming months. Thirdly, we're making bold strategic choices to build stronger brands in a more focused portfolio and, ultimately, to deliver sustainable, profitable growth.

Let me move on to say a little more on trading. Overall, our third quarter has been in line with our expectations. As explained at our interim results, the devaluation of the naira means revenue on a reported basis declined by 24%, but we've seen improved momentum across the business with like-for-like growth improving from plus 2% in our first half to plus 6% in our third quarter.

This momentum has been volume-led with, albeit modest, volume growth in Q3 compared to a decline of 5% in H1. Volume trends improved across each of our three regions. Excluding Africa, like-for-like revenue declined 3%. Again, a slight improvement from the 4% decline in the first half. We've seen particularly strong revenue growth in our UK brands and Radiant in Australia, including the much-anticipated return to growth of Carex, growing by 5% in Q3, with a very healthy balance of price and volume. You'll remember that St Tropez' performance was exceptionally strong in the comparative period, and in addition beauty performance in the quarter has been further impacted by some well-publicised category softness in the US.

As a result of the performance to date, today we're reiterating the full year guidance provided at the interims. On the assumption that the naira exchange rate is broadly unchanged from current levels, we will deliver operating profit for the year in the range of £55 million to £60 million.

Turning now to our cash position, our balance sheet has changed markedly over the past year, given the impact of the devaluation of the naira, and we were clear at our interim results in February that the gross debt of over £200 million was too high. We've made good progress reducing this number since June, and have a clear line of sight to further reduction in the coming months.

Improvements in access to dollars in Nigeria has meant we've now repatriated £35 million so far this year, and with a further £15 million to £20 million expected by the end of the financial year. Albeit subject to FX fluctuations, we'll have repatriated at least £50 million in FY24. This is in line with the guidance we provided at our trading update in November, and we therefore expect gross debt to be in the region of £160 million to £180 million by the year-end, with headroom on our banking facilities of approximately double what it was at the end of FY23.

Accordingly, the board has decided… Also, you'll remember that, for a period of time, we have been disposing the surplus assets in Nigeria, mainly residential property. We ceased this programme in light of the cash build-up and concerns over a potential currency devaluation. However, with greater access to dollars, we have reinstated this activity. In addition, we have identified further assets, inside and outside of Nigeria, which are surplus to our operational requirements.

Combined with the expected sales of recently closed manufacturing facilities in Thailand, as we've previously announced, and land that is no longer required in Indonesia, the value of these assets is likely to reach into the tens of millions of pounds. As indicated this morning, therefore, we can comfortably see a glide path to a meaningful reduction in gross debt compared to the £160 million to £180 million I mentioned a moment ago. In short, we are comfortable with our balance sheet position.

Against that backdrop, I will spend a few moments now talking about our plans to maximise shareholder value through a transformation of our portfolio. Over the last three years, we have made good progress in strengthening PZ Cussons and building back critical capabilities. However, as a board and management team, we are acutely aware that, despite this progress, shareholder returns have fallen short of our expectations.

This is in large part driven by the challenges in Nigeria, which has experienced a currency devaluation of approximately 60% over the last year, but we also consider the overall PZ business portfolio to be too complex for our size. In many ways, we have the complexity of a large global business but without the corresponding infrastructure, resources or benefits that come from scale. As a result, we see financial and human resources spread too thinly to generate consistent returns, and despite the clear strength of many of our brands and our go-to-market capabilities, our competitive advantages are frequently curtailed.

Accordingly, the board has decided to refocus the PZ Cussons portfolio on where the business can be most competitive and where it can create the most value for shareholders. We are therefore taking the following actions. First, we plan to initiate a process to divest St Tropez. The brand has grown significantly under our ownership yet still has enormous potential, not only with its existing customers and proposition but also by expanding into entirely new geographies, categories or channels, stretching far beyond PZ Cussons' footprint. We're passionate advocates of the brand but, at the same time, recognise that more value can be created in the hands of others.

Secondly, we are evaluating options for our Africa business. This is a portfolio of exceptionally strong assets. We have category-leading, indeed sometimes category-defining, brands, highly attractive commercial and manufacturing infrastructure, and a brilliant team with years of expertise operating in these emerging markets. Nevertheless, the board recognises this is a very complex group of assets, and we are therefore evaluating the strategic options both to reduce risk and to maximise shareholder value.

While we are clear on our intention, this process could take some time, and there are a number of potential outcomes. I want to be clear that we will be highly disciplined in each of these processes and are willing to take our time to achieve the right outcome for shareholders. As we stated in the release, the proceeds from any transactions will initially be used to invest behind the organic growth of the business and to reduce gross debt further. The group will also have the potential and ambition to pursue targeted acquisitions which are highly complementary to a more focused category and geographic footprint.

To wrap up, then, a reminder of the three key messages today. First of all, trading is on track with improved volume-driven momentum in Q3. Secondly, with better access to dollars in Nigeria, our balance sheet has improved significantly and we have good visibility in terms of our ability to make further significant progress over the coming months. Finally, we're making bold strategic choices to build stronger brands in a more focused portfolio, and ultimately to deliver sustainable, profitable growth. And with that, Sarah and I are ready to take any questions you may have, so back to Harry.

Operator Thank you, Jonathan. If you'd like to ask a question, please press star followed by one on your telephone keypad now. If you change your mind and wish to withdraw yourself from the queue, please dial star two. And finally, when preparing to ask your question, please ensure that your phone is unmuted locally. And we will just pause for a moment to assemble our roster. As a reminder, that's star one for any questions now. Our first question today is from the line of Damien McNeela of Numis. Damien, please go ahead, your line is open.

Damien McNeela Hi, morning, Jonathan, morning, Sarah.

Jonathan Myers Morning, Damien.

Damien McNeela A couple of questions from me to start with, please. I think if we look at the balance sheet and the gross debt, Sarah, could you just provide a bit more colour? Because if I add up the Nigerian repatriation, there is a gap on your projected gross debt. I'm just wondering how much of the non-trading assets like Thailand fall into FY24 at all, and whether there are any other areas where you've made progress, perhaps working capital to reduce gross debt during the period. That's the first one.

Sarah Pollard Morning, Damien. Good question. What you're rightly pointing to is an approximate 70 million improvement in our gross debt position so far in FY24 with only a 50 million contribution towards that from the repatriation of cash from Nigeria. None of the non-core asset disposals that we are alluding to in the release have yet happened, so that will be an activity over FY25, which is why we're confident for another meaningful reduction beyond that 160 to 180.

So two things have also contributed to the improvement in gross debt in FY24. One is good underlying operational free cash flow outside of Nigeria, and the other is a more determined effort to pool some of our cash balances from our other geographies here to the UK. So all the non-core assets disposals, totalling some tens of millions, are yet to come.

Damien McNeela That's great, thank you very much, Sarah. And then in terms of Africa, obviously it's going to be a fairly sizeable project, I was just wondering whether you could provide any colour on whether you'd spoken to your JV partners yet, and anything you can add there? And also, how does it impact the buyback of the minorities or the threat to the minorities that's currently outstanding?

Jonathan Myers Let me pick that up, Damien, and then I'll pass over to Sarah specifically on the status on the local listing. You're right, it's a big project. It's not a decision that we take lightly, to say that we're going to review strategic options. We're a business with such history and heritage, we've been operating in Africa for 140 years, but equally there's no emotion as we look at this. We have to make the right call in pursuit of shareholder value, and also looking at taking actions to reduce risk for the group.

What we see is a really high potential set of assets, but a quite complex set of assets, including some joint venture partners who absolutely we have alerted that we were going to be making this announcement this morning. And we will be talking to them as we embark on this piece of work, but actually we see the potential for significant value creation in the future in our African business, and we're just trying to explore what is the best option to help realise that. And the local listing is part of the options that we need weigh, so, Sarah, if you just want to [inaudible 00:13:11].

Sarah Pollard I'll give a little more colour on those plans. So, you're absolutely right, Damien, to say that we have announced our intention to buy out our minority shareholders in Nigeria with a view to taking that subsidiary wholly private. We had an offer approved by our local board and put to our local shareholders. The local regulators actually have advised us that they won't recommend that offer proceed due to a local technicality in terms of it being below the prevailing price at which our shares are currently trading in Nigeria. We are equally clear that was an offer that we made in good faith that appropriately values our business there, and we won't be increasing that offer.

If I take us back to the strategic rationale for having made that office in the first place, it was a little bit to take some cost out of the local business that we wouldn't need if we were private. It was far more so to be able to consolidate an income stream at, effectively, an acquisition multiple that represented good economics and value creation for our shareholders. But first and foremost, it was to give us strategic flexibility. So what you should assume is the plans we are announcing today is us taking a more holistic look at the optionality to do exactly that, and give us real strategic flexibility so that our Nigerian business can create value for our group shareholders.

Damien McNeela Okay, that's very clear. And I think perhaps one last one on trading in Europe and Americas. Obviously, you've stated that this year's profit expectation is going to be broadly in line, but just wondering, your conviction on the performance of the UK washing and bathing brands in Q3 and into next year, have you got growing confidence in those brands, given Carex is now back in growth and we're seeing sustained growth across Original Source, Imperial Leather, etc.? Just wondering if you had any thoughts on that.

Jonathan Myers Let me answer that one, Damien. The answer is yes, we have growing confidence, but we also remain healthily paranoid. We absolutely approach it with humility. If you were to look, whether it's on a past-52-week basis or a past-12-week basis, you will see that we have been growing not only value share but also volume share, and actually our biggest competitor has been losing on both counts. So we see genuine momentum across the board with some particularly strong growth rates on brands such as Original Source, such as Cussons Creations.

But we are also able to get to celebrate or mark Carex is back in growth, as we said, by 5% in the quarter for the first time over a full quarter. And that gives us real confidence as we go into next year that we have sustained momentum. But we know that we need to earn that momentum and we need to earn the loyalty of our consumers, so we're working hard to build stronger plans to make sure we carry that through next gear. But yes, we're confident.

Damien McNeela That's clear, thank you very much. I'll let someone else ask some questions.

Jonathan Myers That's, Damien.

Operator Thank you. As a reminder, if you would like to ask a question, please dial star one now. And our next question today is from the line of Matthew Webb of Investec. Matthew, your line is now open.

Matthew Webb Morning, everyone. Three questions from me, please.

Sarah Pollard Hey, Matthew.

Matthew Webb Hi, morning. The first is you talk about investing behind organic growth, and I just wondered if you could give us a bit more colour on that. Is that predominantly in marketing, is it expanding sales teams, it is more recourse into new product development? Any colour there would be very helpful.

The second question is, and I know this is probably quite a difficult one, would you be able to give us any sort of guidance on the likely timetable for the disposal of the various non-core assets that you've both identified and put back into the sale process, as it were?

And the third question, I think the way you've worded it is that you're initiating a sale process of St Tropez, but I just wondered if you had already had any informal discussions, expressions of interest, anything that would encourage you that an attractive price can be achieved and, perhaps more broadly, whether you think there's a healthy market out there at the moment for this sort of asset? Those are my three, thank you.

Jonathan Myers Very good, Matthew. Why don't I take the first, and Sarah can pick up on the second, relating to the M&A timetable. First of all, we absolutely see an opportunity with a healthy return in investment lens that we believe we can generate returns on investing behind some of the very strong brands that we have in our portfolio. We approach it in two ways. What is sufficient to be competitive? And then what is the activity we will be investing behind, and does it merit the investment?

So we want to get enough oxygen into the P&L, ideally through gross margin and managing price mix so that we have the ability to invest and still maintain a healthy P&L structure. But then, before we release that investment, are we actually sure that what we're going to invest behind has got a track record, proven return?

It could well be in marketing, so yes, classic media. It could also be in the form of innovation, and we have made some structural changes over the last six months to put greater focus behind innovation capability, so we build a richer pipeline of future innovation that we have more confidence, through good pre-market or pre-launch qualification, will give us a bang for our buck, but actually goes beyond marketing and innovation.

We're also thinking, potentially, in some digital data activation, but ideally also, as we strengthen our go-to-market capabilities, so that we have a real winning face to the customer base that we're dealing with, whether it be in the UK or in Australia or any other markets we operate in. But we'll always be applying a rigorous ROI lens to make sure we're not eroding value, we're actually generating value. Sarah?

Sarah Pollard Morning, Matthew, thanks for your question. You would expect me to not be drawn on timetable for the processes that we've announced today for one overarching reason, and a couple of specifics. One is we're clearly going to be very disciplined and we will not be trading off speed for value, so you shouldn't expect us to be in a rush through that lens, and the teams on the ground are very much focused on maximising and optimising all of our businesses as they remain in our care.

The St Tropez separation will be relatively more straightforward if you think about it being a single brand in, effectively, a single market. We generate about 70% of our St Tropez business in the US. In Africa, first and foremost, we have no predetermined outcome from valuation that we've embarked on, but any option we pursue will be slightly more involved.

So let me not be drawn on timings beyond that, but that absolutely is the reason that you see us talking about initiating the separation and the sale of the St Tropez brand. That said, you should assume they are more than plans on a piece of paper. We have actually, over the last two or three years, let alone the last two or three months, received a number of legitimate and unsolicited interest in various parts of our business.

And particularly you, as well as I, can look to the beauty sector particularly to know that there is a good, healthy level of interest in high-quality beauty brands, which we absolutely passionately believe St Tropez to be. So let me not be more specific, but we are confident in the outcome of both of those processes realising shareholder value for us at PZ Cussons.

Matthew Webb Thank you very much, very clear.

Operator Thank you. This will be the final reminder for questions. If you'd like to ask a question today, please dial star one now. Thank you. And this will conclude the Q&A session, so I'd now like to hand back to Jonathan Myers for any closing remarks.

Jonathan Myers Okay, Harry, thank you very much. Thank you, all of you, for joining us this morning. Obviously, it's way more than the scheduled Q3 trading update, given the news that we have announced. As and when we have more to say, we will. We're not going to give a running commentary, but we will obviously be keen to update you when there is appropriate news.

Of course, if you do have questions, following what we've announced, you can follow up with us, or you can get in touch with Simon. Otherwise, Sarah and I have plenty to get on with, so that's what we're going to do, and we'll leave you to get on with your days too. Thank you very much.

Operator Thank you, everyone. This concludes today's call. You may now disconnect your lines.