Chr. Hansen

Q2 results 2016/17
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Operator: Thank you for standing by. Welcome to the presentation of Christian Hansen's results for the first half of 2016/2017. At this time, all participants are in a listen-only mode. There will be a presentation followed by a question-and-answer session, at which time if you wish to ask a question you will need to press star one on your telephone keypad. You are also welcome to submit questions via the web by clicking on the Q&A tab in the webcast at any time during the call. The questions submitted via the web will be answered after the call. I must advise you this conference is being recorded.

I'd now like to hand the conference over to your speaker today, CEO Cees de Jong. Please go ahead.

Cees de Jong: Thank you, operator. Good morning, and welcome everybody.

I'm Cees de Jong, CEO of Chr. Hansen. And with me is our CFO, Soren Lonning.

Now before we move into the presentation, let me just say that I'm very pleased with the solid performance in the first half of our current financial year '16, '17. And looking at the second quarter, all of our 3 business areas delivered strong growth. Health & Nutrition even did a little better than we had expected. And we're now very well positioned to deliver on our ambitions for the year.

Now please move to the next page and take a look at the disclaimer. I hope you have had a chance to read the statement, or we will do so afterward. So let's move to Slide #3, please.

Looking at the numbers for the first 6 months, revenue increased by 13% to just over EUR 500 million, and this corresponds to an organic growth of 10%. In Q2, we delivered 9%, and as said, this was driven by all 3 business areas. The organic growth for the first 6 months was driven by 8% from volume and mix, while price contributed around 2%. There was no contribution from price in the second quarter, as the impact on organic growth from our euro-based pricing model turned negative in that quarter. And that was driven by the strengthening of the Brazilian real and the Russian ruble against the euro. For the full year, we expect the impact of euro-based pricing to be modest.

Food Cultures & Enzymes delivered organic growth of 9% in the first half of the year, with strong growth in fermented milk and in cheese. The growth in fermented milk was to a large extent driven by continued good momentum in China, and that is for various types of yogurt and fermented milk drinks. And in cheese, we continued to a see positive impact from conversions in the United States. In the second quarter, the organic growth for Food Cultures & Enzymes reached 8%. The organic growth in Health & Nutrition was 10%, and it was driven by strong growth in the second quarter of 13% which was better than we expected. The growth was mainly due to animal and plant health, but human health also delivered strong growth. The strong performance in animal health was very encouraging. And it was driven by us winning customer projects, especially in silage and in poultry. The general markets are improving, but conditions are still challenging. And our dairy cattle segments, as an example, did see sales below last year.

Now in the first 6 months of the year, Natural Colors delivered 11% organic growth, with volume and mix contributing around 5% and price 6%. The volume growth was affected by our ongoing efforts to improve profitability, and we aim to achieve that through simplifying our profit portfolio and through a strict pricing policy. Now we do expect to see these initiatives keeping growth down in the coming quarters. And we also monitor this closely to ensure we maintain our competitiveness in key markets.

For the group, the operating profit before special items increased by 15% to EUR 136 million. And with that, the EBIT margin before special items was 27.1%, and that is up from 26.6% last year. The increase reflects the positive impact from operational efficiencies in Food Cultures & Enzymes and the profitability initiatives in Natural Colors, whilst the EBIT margin in Health & Nutrition remains below last year as lower scrap levels were more than offset by higher depreciation and amortization from acquisitions and increased R&D activity. In Q2, the EBIT margin before special items declined by 0.9 percentage points, driven by one-off costs related to the change of management that we announced in January. In addition, EBIT was impacted negatively by the extra costs incurred for initiatives to secure full utilization of the existing production capacity in cultures ahead of the new capacity expansion planned to be ready in the fall of 2017.

R&D expenditures amounted to EUR 36 million or 7.2% of revenue, and that compares to 7.5% last year. The decline, relative to revenue, was driven by costs related to the acquisition of a strain collection from the Dairy Innovation of Australia, and that happened last year, as you'll remember. Excluding this, we continued to expand our investments into R&D.

Profit for the period ended at EUR 98 million, up 28% from last year. And finally, the free cash flow before acquisitions and special items reached EUR 30 million, which was almost twice as much as in the first half of '15, '16.

Let's move to the next slide for an update on the strategic highlights of the first half year. As you know, we've identified 3 strategic initiatives, and internally we also call them lighthouses, to support the long-term growth of Chr. Hansen. And I am pleased to see the continued good progress across all 3 of these. In bioprotection, we continued to see strong growth. In the first half of our current financial year, growth reached approximately 25%. And as you know, bioprotection accounts for about 5% of the revenue in Food Cultures & Enzymes. In plant health, we saw strong growth in Nemix C, and we continued to see encouraging field trials supporting the penetration of the product. Outside Nemix C, VGR continues to hold good potential, but as for Nemix, it has a long introduction period. And that, of course, is not unlike our introduction of new innovations in a large business area in dairy. Within the human microbiome, working in our new microbiome center, we've succeeded with process development for the first strict anaerobic bacteria, and that is for a third-party product that has pharmaceutical potential. Now although it's early days for activities in microbiome, I think the result is a big step forward for our efforts in this field.

We're also progressing well on the expansion of production capacity for cultures in Copenhagen. As I've mentioned, we've taken a number of initiatives to safeguard production volumes until we start operation in the autumn of this year. We've seen and we continue to see a strong demand from Asia, especially China. And that's very positive, and also the result of our decision to go direct a few years ago. But due to this positive development and continued growth of cultures, it's been necessary to add to our logistics cost so that we can secure delivery performance. Running at full capacity also means that we've reached a point where it's difficult to reap benefits of scale, as we right now do not have the flexibility to optimize our production processes until we have the new capacity fully implemented.

Our animal health business overall does very well despite market conditions that are only gradually improving. The beef cattle segment, which we entered with the NPC acquisition, is one of the areas where we still are negatively impacted by the challenging market conditions. With that said, we continue to progress on the insourcing of production and have started to see this impacting our results positively.

The integration of LGG is ongoing, but let's take a closer look at this on the next page, Page #5, please. Here I'd like to spend a few minutes on the opportunities that we now have with LGG both in fermented milk and also on human health. And as all of you know, LGG is the world's most documented probiotic strain, and the science continues to strengthen with new studies being published every year. Together with our own BB-12, we now have a unique offering with the world's 2 most documented probiotic strains as well as strong documentation on the combination of the 2 strains in both gut health and immune health. And that means that through the acquisition we will be able to fully leverage the potential of the LGG brand both as a stand-alone product and in combination with BB-12. In Food Cultures & Enzymes, we can expand our probiotic offering and better target some of the faster-growing categories such as children and millennials. And for them, for that age group, LGG has very strong documentation. And we already see strong interest from customers in most of the regions. In Health & Nutrition, we have a number of opportunities to release the full potential of LGG with our microbial and market understanding. We are currently strengthening our strategic partnerships by offering exclusivity for key markets in both dietary supplements and infant formula. And to further build out the position of LGG, we are differentiating the strain, and we do so more against generics, by utilizing key opinion leader networks from both academia and health care. Building a brand around LGG together with our strategic partners is the final priority. It will strengthen the link between the market-leading clinical evidence and the LGG trademark, and this enables consumers to make intelligent choices.

Now let's move to the next slide for an update on the regional performance in the first half of our year.

Returning to the development in the first half of the year. We delivered 6% organic growth in the EMEA region. The growth was supported by both volume and price; and was broadly based across most of our businesses but especially in bioprotection, Natural Colors and cheese. In the second quarter, the organic growth was 3%, slightly negatively impacted by our euro-based pricing model in Russia and a negative development in fermented milk and animal health. The development in fermented milk was partly driven by unfavorable conditions in certain markets but also customer-related order patterns.

In North America, we saw 12% organic growth. And there was strong growth across all segments, except fermented milk and enzymes which showed more modest growth. In cheese, we continue to see a good progression in conversions with a number of customers, while animal health was positively impacted by customer wins. Organic growth reached 17% in North America in the second quarter. Latin America delivered 9% organic growth, with growth supported both by volume and price. And we did see strong growth in cheese, Natural Colors, animal health and plant health, while probiotics were below last year. In the second quarter, organic growth was 4%. And the organic growth was negatively impacted by the euro-based pricing due to the stronger Brazilian real but also by tough market conditions.

APAC delivered 17% organic growth. And we saw strong growth in fermented milk including probiotics, but also in cheese, enzymes, human health and in animal health. Only growth in Natural Colors in Asia Pacific was more modest. The strong growth in fermented milk continues to be driven by China. And organic growth in Asia Pacific reached 18% in the second quarter.

And with this, I'll hand over to Soren to go through the financials of each of our businesses.

Soren Westh Lonning: Thank you, Cees.

Let me start with Food Cultures & Enzymes, where we continued to see solid growth in Q2 of 8%, although slightly lower than in Q1, bringing the organic growth for the first half year to 9%. All of the 8% in Q3 -- Q2 came from volume and mix, as the impact from euro-based pricing has turned against us in Q2 due to the stronger Brazilian real and Russian ruble. The volume growth of both the first half year and Q2 was primarily driven by cheese, fermented milk including probiotics, meat and wine, with all segments, except wine and probiotics, being supported by our bioprotective solutions. Bioprotection as a subcategory delivered growth to the tune of 25%. Enzymes, on the other hand, showed modest growth in line with the global cheese production.

Turning to the EBIT margin. Then in Q2, we did see a reduction in margin by 1.6 points, which primarily was due to one-off costs related to the management change that Cees mentioned earlier. The impact from this was around 1.5 percentage points. We did still see a positive impact from underlying operational efficiency, but it was all offset by initiatives to secure volume ahead of the new capacity coming live in the autumn, including shipping more goods with air freight rather than sea freight. Also, we did continue to invest in R&D and sales and marketing, primarily for the bioprotection initiative. Looking at the first half of the year: We have delivered a margin expansion of 1 percentage point. This has been driven by operational efficiencies, although partly offset by initiatives to secure full utilization of existing capacity and higher R&D activity. The negative impact from the management change in Q2 was offset by the income from a property sale in Q1 this year and easy comparable in Q1 last year from higher administrative costs.

Let's turn to the next slide and look at Health & Nutrition, which did better than we initially expected, with organic growth reaching 13% in Q2 and 10% for the first half of the year, thus now being in line with our long-term ambition of double-digit growth. The good performance in the first half of the year was driven by both animal and human health. Animal did well, especially in the silage and poultry segments, mainly from new customer and project wins and a continued restocking of silage ahead of the 2017 season. The dairy and beef cattle segments remain weak. However, markets are gradually improving, with milk prices back to a more normalized level. Human health showed a solid growth and is ahead of our original expectations, as we have managed to accelerate a number of projects which we had expected only to materialize later in the year.

The EBIT margin ended 0.8 percentage points below last year, in Q2, driven by higher depreciation and amortizations from acquisitions and increased R&D activity, whereas a continued low scrap level in human health and insourcing of NPC products added positively to the margin. It is also worth mentioning that we did have a 6-month impact from the U.S. duty cost in Q2 last year, which made the comparable easier. For the first half year, the margin is still down by 2 percentage points. On top of the margin drivers in Q2, the year-to-date margin remains impacted by timing of factory maintenance in Q1 this year and changes in inventory levels.

Please turn to the next slide. Natural Colors delivered 9% organic growth in Q2, with volume/mix contributing 5 percentage points, and price 4 percentage points. For the first half year, the organic growth has reached 11%. The organic volume growth was primarily driven by strong growth in the natural carotene, annatto and anthocyanin pigments, while carmine volume continued to decline due to profitability initiatives. Growth was anchored across most industries and especially driven by EMEA and North America. The impact from pricing came down a bit, as the raw material prices for carmine has been declining. This is how they were partially offset by increasing prices for annatto seeds used in many of our orange shades.

The EBIT margin increased by 0.6 percentage points in Q2, driven by the ongoing optimization initiatives, including reduced logistics cost, partially offset by one-off costs related to the initiation of these initiatives. Looking at the first half year, then margin is up with a healthy 1.6 percentage point driven by margin and mix management as well as logistics optimizations.

Let's move to the next slide.

When looking at the group results for the first half-year: We have delivered 13% growth in revenue measured in euro, which equaled an organic growth of 10%. Volume and mix accounted for 8 percentage points. Prices grew 2 percentage points, while acquisitions added another 3 percentage points. The net impact from currency was close to 0. EBIT before special items was up by EUR 18 million, leading to an improvement in EBIT margin before special items of 0.5 percentage points to 27.1% for the period. EUR 1 million in special items related to the LGG has been incurred year-to-date.

Let's take a closer look at the cash flow on the next slide. The cash flow from operating activities improved by EUR 15 million, while the cash flow used for operational investing activities increased by EUR 6 million largely due to investments in capacity for culture production. All in all, this resulted in a free cash flow of EUR 23 million. On top of this, we have also spent EUR 73 million in Q1 on the acquisition of LGG and the related business. The capital expenditures excluding the acquisition corresponded to 9.9% of revenue, which was well above last year as we have stepped up the investment level. Return on invested capital excluding goodwill increased by 0.9 percentage points while the net interest-bearing debt-to-EBITDA ratio was down to 2.0x despite the acquisition of LGG.

Please turn to the next slide.

The results for the first half-year gives us good comfort in maintaining the outlook for the year of 8% to 10% organic growth and a slight increase in EBIT margins compared to last year. Looking at the growth in the second half versus the first half of the year, we do expect to see lower growth for a number of reasons. Growth in Natural Colors is likely to be slightly lower than in the first half due to a tougher comparable, especially in Q3 and based on the assumption that for the full year the impact from raw material prices will be close to neutral compared to last year. We do see growth in cultures in China to ease off a bit. Momentum is still strong, but we will face a higher comparable in the second half. And finally, we do expect the euro-based pricing to be slightly negative in the second half. The free cash flow is still expected to be around at the same level as last year due to higher investment level.

And with this, I will hand over to the operator to start the Q&A session.

Operator: Thank you. We will now begin the question-and-answer session. If you wish to ask a question please press star one on your telephone and wait for your name to be announced. If you wish to cancel your request, please press the hash key. Please stand by. Your first question comes from Soren Samsoe.

Soren Samsoe: It's Soren Samsoe here from SEB. First, a question regarding your guidance, 8% to 10% growth. I was just wondering if you could elaborate a little bit on which kind of uncertainties that should materialize if you should not reach the 10% growth given that you have already reached 10% in the first half.

Secondly, if you could tell us when -- from what quarter we could expect the new fermenter to be up and running and adding again to scalability effects. And then also, regarding your sales and marketing costs, I'm just wondering. I can see they are up 23% in the first half. Just if you could tell us a little bit about why it's up so much.

Soren Westh Lonning: OK, Soren, I will take -- address your questions. So in terms of the guidance, the 8% to 10%, we have already spoken to what will take the growth -- would impact the growth momentum that we have seen in the first half, definitely in the second half. That is, as mentioned in the call, it is natural color which have a tougher baseline and where we have seen raw materials coming down. So we've had a positive impact from raw material price increases in the first half, and that will be negative in the second half with the existing prices that we know of, so to become net neutral on the year. So that's one key thing. The second part, that is you can say, China as we mentioned. This is basically pure mathematics. As we become larger and larger in China, and we are now -- also we had some substantial wins and expansions in our customers during the first half of last year. Now we are facing a tougher baseline and just a much larger base to grow on. Then we will also see organic growth. Although still very strong, it will come down a notch compared what we have seen in the first half. And then finally, euro-based pricing, it has been slightly positive in the first half, and that will turn slightly negative in the second half. And so those are the 3 dimensions that will change from first half of the year to second half of the year. In addition from what we guided earlier, we have said that we will be back-end loaded in Health & Nutrition. We still expect very good growth going forward, but we have also been able to actually accelerate some of the customer projects that gave some uncertainty, so we have already now seen some of the benefits from that. So those are the key drivers of this. Then if I shall address your second question, in terms of the new fermenter, we expect that to be up and running by the -- probably towards the end of Q1, but of course, it can change a little bit. Now normally when we bring new capacity online, you will not see a large scalability effect from the beginning because it takes a little bit of time to ramp it up fully and we start depreciating on the assets immediately. So it will still take a little bit of time before we will see scalability from that, but as we've said earlier, '19, '20, '21, we will see clear scalability from the production expansion here. And then, sorry, the third question, could you repeat that, Soren?

Soren Samsoe: Yes. It was just on the sales and marketing costs that are up 23% in the first half year-on-year, why it's up so much.

Soren Westh Lonning: Yes, yes. One key driver here is the NPC acquisition in the first half of the year. We didn't have NPC last year. And most of the resources that we took over here was actually sales and marketing resources, so that drives quite a substantial increase. In addition, of course, we are also investing in -- Soren, you can say, in the organic part of the business. We are adding more resources behind bioprotection in emerging market et cetera, so that is sort of securing a certain base growth in sales resources. But the NPC is what really drives the un-normal high increase.

Operator: Your next question comes from Annette Lykke.

Annette Lykke: First of all, when we look at the EMEA growth, it was just around 6%. I'm just wondering if you could elaborate a little bit on how you see this for the second half or if this is sort of a new normal level you see here. And then in respect to the capacity expansion you have, I think that last call, you indicated that it would last at least for something like '20 and '21. If you can be more precise on that. And also, let us know when you think you will have to start investing in a greenfield capacity after this -- you have completed here, just to know when we need to see your CapEx going up again.

Soren Westh Lonning: Yes, in terms of the EMEA question, I'd -- we are actually pleased with 6% organic growth in a relatively mature market like EMEA. Now we have for a period of time been fortunate in Food Cultures & Enzymes by a relatively high cheese production. That is normalizing in EMEA right now. We've also had some tailwind from euro-based pricing due to the Russian ruble and the Turkish lira having depreciated. That has actually turned against us now. And then finally, we do have quite a sizable carmine business in EMEA. And here we have also had that, on the organic growth, tailwind from that (pilot) increase. Now it's actually reducing, so it's taking the growth down a notch. So I would say there are a few things that are changing, but we are still pleased with 6% growth in EMEA. In terms of the new capacity, then I will be cautious to give an exact date as to when we -- when it will launch, the new capacity, but we are talking beyond '20. It could be around '22, plus, minus, depending on what volume growth we will see in dairy culture. So that's the time. And then we will start to invest 1 to 1.5 years ahead of this, start to ramp up investments. And now we haven't -- just to repeat that message, we haven't decided where or how we're going to make an investment in the expansion in this line. We know that the current model that we have in there cannot easily be expanded, but we haven't taken any decision as to where and how so that is still open. And we have time to really make a thorough analysis of that before we conclude on this.

Annette Lykke: OK. Just to confirm, the negative headwind you're seeing on euro-based either from Russia or the carmine prices, that's just carry-through, that's right.

Soren Westh Lonning: That's -- the raw material prices in natural color, that is, if we are agile enough in terms of our pricing behavior, then it doesn't have an impact in EBIT. And that's normally what we see. There can be small timing effects of it, but we normally price out quite well on these things. But we also have to make concessions when raw materials go down. So this is an organic growth impact that really doesn't have an effect on our EBIT margin structurally. On the euro-based pricing, I mean, this is -- this relates more to protecting the business when we see depreciating currencies. So again, here it will not -- it will normally not have an effect on our absolute EBIT measured in euro, as we have exactly protected the business. And just to -- on the size of this, close to plus 0.5 percentage point in the first half and close to minus 0.5 percentage point in the second half. That's roughly the dynamics we have for the group, not EMEA specific.

Operator: Your next question comes from Heidi Vesterinen.

Heidi M. Vesterinen: So I have three. First of all, in Natural Colors, how much do you think you would be growing in volume terms if you didn't have your margin initiatives? And when do these initiatives come to an end? Is it 2018? And the second one, in the release you talk about a positive inventory effect in Cultures & Enzymes in Q2. Can you talk about what happened and possibly quantify it? And then a last one, I wanted to ask about bird flu. We've seen some incidents recently. And how does that impact your business? I wondered if that might make customers somewhat hesitant to take on new products. What actually happens on the back of that?

Soren Westh Lonning: Yes, Heidi, let me address your 2 first questions. And then Cees will address your third one. Now I think it's important to state, when we talk about the natural color and look at the volume, just split it into also a carmine and non-carmine business. We are actually growing double-digit volume-wise outside of carmine, so within that category, we are doing quite well. In the carmine segment, where we have had the highest focus on profitability over the last 6 months, here bear in mind that last year, we -- there was a shortage of carmine. And it also meant that we could take some business that was simply at higher margin than it normally would be last year. And now this margin -- with the changes that we have seen now, margin is coming back to normal in some of these business types. And here we are simply just saying we will not -- we are here to earn good profitability on all the business that we do, so we have simply been more hard in this particular product segment. So you have to differentiate the volume development between those 2 categories. In terms of the Food Cultures & Enzymes and -- it's right that we -- it's true that we in the Q1 had some timing effects. Now we've had the production shutdown in the -- in Q2 in order to prepare for the capacity expansion, meaning that we did not face a similar size impact from inventory and timing of costs in Q2, meaning that the effect in the first half of the year is less than 1 percentage point favorable from timing and cost, inventory buildups and the likes.

Cees de Jong: Heidi, let me take your last question, on bird flu. And that, of course, is quite an interesting one. And first, let me say that the second quarter growth in Health & Nutrition, in animal health, was of course in part also driven by us making advancements in poultry, but generally when it comes to bird flu, I would expect to see an impact only when flocks are being destroyed, so to speak, because of the bird flu. We've not seen sort of a general trend where it impacts our sales either up or down.

Operator: Your next question comes from Lars Topholm.

Lars Topholm: Lars Topholm from Carnegie. Just a couple of questions. You mentioned the higher transportation costs. And I assume that those have to do with where you produce but also that air cargo rates soared. Can you try to quantify, isolate this margin effect on FC&E from higher transportation costs? And then a question on LGG because from value you also have got transglutaminase enzyme technology. Can you put some comments on, if that's something that could be significant, what is the timeframe to commercialize this? And then finally, just out of curiosity, when you mention growth, you talk about strong growth in some cases; other cases, solid growth; and then also good growth, even modest growth. I think, modest growth, I understand, but can you please explain to me how I should think about the other 3 phrases?

Soren Westh Lonning: OK, I think I'll take, I'll address your questions, Lars. In terms of the freight, and I'm not giving exact, but we are talking somewhere around 0.5 percentage point in Food Cultures & Enzymes. And it's driven by the fact that we -- both it's a more expensive mode of transport and it's also because we need to transport more around our 3 main dairy culture production sites because we are simply running at such high utilization that we need to optimize this, its movement around goods, that way. So it's 2 things, but you also need to be aware that we are also -- that's not the only thing that drives higher costs. It is also that we need to work with -- put more expensive (ships on). We need to utilize all the capacity that we have, also moving into smaller fermenter sizes once in a while. And we are also ramping up some employee hirings that we would otherwise have done a little bit later as part of the '17 ramp-up in the new financial year. So freight is not the only component. There are also other components that have a negative impact when you run this almost 100% utilization. So that...

Lars Topholm: So what you -- would you estimate the net drag on margins to be from all this, just in ball figures?

Soren Westh Lonning: We'll -- it's -- look at something that is around 1 percentage point negative, maybe slightly more and -- but it's around that.

Cees de Jong: Let me take your second question, Lars, on TG. In all fairness, there we are still investigating the opportunity. What we mentioned during the call, of course, is our enthusiasm on LGG and the combination of LGG and BB-12. And I hope that you're all aware on the call about the power of LGG. So many clinical trials done in young children, for instance, with LGG show a reduced risk of what's called the upper respiratory tract infections. So we would say common colds. When you give LGG to, let's say, young children, day-care-age children, that risk can be reduced by 36%. The combination of BB-12 and LGG is known in young adults. There was a great study done in college students. And there what we could see is that both the duration of, let's -- again, for let's say the common cold, upper respiratory tract infection, duration, we could reduce by 1/3, as well as the severity. So we're really very enthusiastic that we've now got both the race horses and probiotics in our stable. Soren, do you want to take the question on growth?

Soren Westh Lonning: Yes...

Lars Topholm: Yes, sorry, Cees, can I just do a follow-up on -- well, I mean actually not probiotics but human biome. So your anaerobic fermentation breakthrough, is that in any way related to trying to prevent Crohn's disease?

Cees de Jong: No, it's not, Lars, no. It is a strain for a third party. And I don't think I'm at liberty to disclose what they're targeting, but the fact that we've been able to produce and stabilize that strain which is a strict anaerobe, I think, is a very significant achievement for the team up here.

Soren Westh Lonning: And then your third question, Lars, let me address that, strong, solid, good growth. We -- the ranking of these words is strong obviously is the best; solid, second best; and then good following after that. And what we, with these, try to indicate is also how we are performing compared to, you can say, our long-term financial ambitions. So if you look to Food Cultures &

Enzymes, then we are riding a solid growth in Q2 of 8%. That is in the upper end of our long-term financial ambition. If it would have been 10%, we would have called it strong growth. So that's a very short translation of what we're thinking or mean by these words.

Operator: Your next question comes from Michael Rasmussen.

Michael K. Vitfell-Rasmussen: Could you add a little bit more on what is causing the slowdown on fermented milk in North America? Is this competition growing? Or is there anything on the consumer side which we should be aware of? My second question goes on China. What is your current forecast of the underlying yogurt market growth? And can we add anything interesting in terms of which categories are outgrowing the total market? And finally, on LGG, can you talk a little bit about the potential for top line synergies now that you know the company a little bit better?

Cees de Jong: Thanks, Michael. When it comes to North America, and to some extent it's also Western Europe, what we see is that leading brands are -- in fermented milk and yogurts are not growing because the innovation levels are poor. We don't think that underlying demand is affected. Very often the space is taken by smaller brands. And that to some extent helps us, but it is showing that part of our growth, a more important part of our growth, in future for fermented milk will come from emerging markets. And I'm very pleased that when we launched Nature's No. 1 back in 2013, we earmarked this as one of the key areas to work on to strengthen our position both technologically as well as from an infrastructure and capability point of view in those emerging markets. And that's exactly what we did. And then, that of course, is a nice lead into China, which is basically showing that approval was the right decision to move in there with quite some force. When we look to the Chinese market, let's say, in the most developed areas, let's say the coastal cities, what we now see happening is that we see sales into, let's say, the more advanced type of products. We see the quality of fermented milk products go up. And that gives us an opportunity to do up-selling, where if you would go to the more inland cities, there it is still a volume game. So that means that going forward we definitely have not seen the end of the growth in China yet. We're still very positive about it. And then your third question was on LGG and top line effects. I think what we've been guiding before is that about 0.5% to 1% for human health and Food Cultures & Enzymes is the guidance, and it's what you should think about.

Michael K. Vitfell-Rasmussen: OK, so no positive or negative surprises on that side.

Cees de Jong: Definitely no negative surprises. And what we're doing -- maybe to elaborate on that, what we're doing is we're closing down some smaller contracts that the previous owner of LGG had made so that we can really leverage the brand with real large players.

Operator: Your next question comes from Hans Gregersen.

Hans Gregersen: Three questions. And turning to Food Cultures & Enzymes: You had a few comments previously on the running of the new capacity, where you said it will go online towards the end of the year. Does that mean the entire capacity is ready to run at full speed? And in that context, I sense that what you're saying right now is that you are actually losing business or you're not able to grow the business as strong as you could given the capacity constraints you have right now is the first question. Second question, you mentioned that non-carmine products were growing double digits. And you also mentioned in the report that certain raw materials are starting to increase. Am I right to assume that given you have a far more diversified product mix today, i.e. carmine has declined, that you are less sensitive to individual price moves in raw materials? And then finally, on the biopreservation, can we provide a little bit detailed trading update? You mentioned it's still growing 25%, but where are you growing in terms of product, regions, et cetera?

Soren Westh Lonning: Thank you, Hans. Let me address your first questions. So we -- on the expansion in the Copenhagen sites in food cultures production, we expect, as said, to have completed this during Q1 of the financial year '18. You will not run full speed from day one. You will normally fill the capacity up by, let's say, 50%, to that tune. And then you will start working with this, and then you'll gradually ramp up. We're also in a situation where we don't need to bring in the full capacity. Bear in mind that we are doubling the fermentation capacity in the Copenhagen site. So that's not a -- it's not a challenge for us, that it's -- you start lower than food utilization. And it's not -- we have not lost business due to the capacity situation we -- here. That's important to emphasize. We are in a -- we have been in a situation where we could see a limit to the upward potential in Food Cultures & Enzymes vis-ˆ-vis our guidance of 7% to 8% organic growth, but we have actually worked, and large credits with the production team, in handling both producing at full, maximum utilization while running a major expansion project at the same time. We are actually in a situation where this has been executed very well, and we are following the plan exactly. So we haven't lost any business in the market due to that, but what we have said earlier was there was a limit to how much we could grow this year in Food Cultures & Enzymes but we have not hit that. And...

Hans Gregersen: But not -- what you're saying -- sorry for interrupting. What you're saying is that you have not lost customers but you might have been forced to say no to potential new orders and new customers.

Soren Westh Lonning: No, no. We haven't said no to new business as a result of this, but what we have said is, if we are suddenly growing at a completely different level in Food Cultures & Enzymes compared to the 7% to 8%, then we could run into challenges. But that has not been the case.

Cees de Jong: And maybe to add one thing to -- Hans, for your understanding. And it's also a little bit of insight in the EBIT development there. Sometimes, today, our delivery performance is not at the level where we want it. And that has to do with the fact that we are running at full capacity, but obviously, we're not turning business down but I will say we're also not bending over backward to make it happen for customers. And that means that, sometimes, smaller customers suffer a bit due to the fact that we run at maximum capacity. That's, of course, not a situation we want to be in. Do you want to take the carmine?

Soren Westh Lonning: Yes. Let me address the carmine. You are right, that we are to a certain extent less sensitive to a single pigment. Carmine is still our largest pigment in natural color, but it is less than 20% of revenue. And it has come down since this was a topic 4, 5 years ago. And so it has been reduced. It's also important to say that the carmine price increase that we have seen this time has been clearly less than it was these 4, 5 years ago. At that point in time, we reached a price level of USD 120 per kilo of raw material input. And that peaked at $60 last year, so it hasn't been as big either. So both parameters go into the equation.

Cees de Jong: Let me take, Hans, if that's OK, your question on bioprotection. First half of the year, we indeed grew 25%. And bioprotection is now about 5% of Food Cultures & Enzymes sales. And if you would want to model this, you would have to take into consideration that the traditional spaces where we operate in, so it's fresh dairy, cheese and meat, by far, take up the growth. The sales that we have in the other segments are still relatively small. And also, when we look at where the growth is going to come from in the next 3 years, it is those traditional fields where we still see a very significant demand. Interesting to note that, whilst some of our competitors seem to take their foot off the gas in this field, we've just seen another one enter. And they use exactly the same words and the same pictures that we've been using in the field, so we feel flattered that we're being copied.

Hans Gregersen: You mentioned previously that you're looking at, let's -- salmon and fresh salads et cetera. And you said we are a little bit hammered by regulation. Are there any improvements in regulation at -- of adopting this new technology?

Cees de Jong: I don't think I said we are hammered by regulation, but I -- well, what we did say indeed is that regulation in certain cases needs to be adjusted and adopted. That is always a process that takes time with regulators because obviously, they can't take chances. They need to be convinced that what's happening is the right thing. The only answer and the other perspective I can give there is in certain countries indeed regulators are making the changes. In other countries, that's going slower. And that obviously it's why we're a little bit more cautious on the fields outside fresh milk, cheese and meat. However, we do make first sales in salmon and salads, as we were alluding to before. And the last thing

I'm going to say about that, look at what we're doing. We're replacing artificial chemicals with all-natural-material solutions.

Operator: Your next question comes from Arthur Reeves.

Arthur John Reeves: Could you just give us a bit more market background? You talk about the cheese market slowing down from 3% to 2%. Are there particular areas of the world where that's happening? And in Natural Colors, has the pace of change from companies wanting to take out artificial colors increased or decreased in the half year, please?

Cees de Jong: Arthur, let me take your questions. What we've seen obviously in the European Union is that a lot of additional milk had become available in '15, '16. And quite some additional cheese was produced. I mean, when there's so much milk, you need to make sure you can store it. The only way you can store it is either powder or cheese. That has given us quite a bit of help in those years. By now, the markets are back to normal levels, and that means for cheese it's around 2% growth, Europe probably 1.5%, the other markets a bit faster. Overall, we would expect that level to continue going forward. What we see in Europe is the ability to export cheeses. And that's actually a testimony to the power of that industry. When -- your second question was, remind me again, Arthur, on...

Arthur John Reeves: Around Natural Colors and whether people are stepping up the pace of taking out artificial colors?

Cees de Jong: Yes. Sorry. No, actually what we see in the United States is that conversion is happening. And I think we're extremely well positioned to take our share due to us working with a significant number of the very large players. I mean we've been endorsed by one of the largest QSRs to work with with their suppliers. We work with some of the leading brands. And I think it's fair to say that, of the projects we take on, we win about 1/3. So that goes quite well. What it means in terms of sales for Natural Colors, where we do grow double digit in North America, that in 2017, as we said before, we will see the impact of that conversion.

Arthur John Reeves: Is it happening faster in North America than in Europe?

Cees de Jong: As you know, Arthur, Europe had started this conversion already many years ago, after the (inaudible) study in -- I think it was 2007. So here in Europe, we have regulations in place that enforce the food and beverage manufacturers to label their product if they still want to use certain chemical colorants. There is no such legislation in the U.S. In the U.S. it's purely driven by consumer demand. Operator, I think we have time for one last question.

Operator: We have a question from Klaus Kehl.

Klaus Kehl: Klaus Kehl. 2 questions. First of all, you mentioned that you have some extraordinary costs in Q2 in Food Cultures & Enzymes due to management changes, but could you quantify that impact and -- or at least, yes, confirm that -- what I have calculated, that it must be in the range of EUR 2 million? That would be my first question. Secondly, you mentioned that you have these higher distribution costs in Q2. And I guess what you're saying is that we should expect that to continue in the second half of the year. Is that correct?

Soren Westh Lonning: Yes, let me address these, Klaus. So the EUR 2 million is a very good estimate. And when you calculate that, it means that in Food Cultures & Enzymes, the reduction that you see in Q2 in margin of 1.7%, that is 80% to 90% driven by this event. And so that's a quite material impact in this business area. When you look to the higher distribution, you are right. We are expecting the higher costs to continue in the second half of the year. And that's also why we -- when you look, we are at plus 1 percentage point in margin expansion in the first half of the year. This is also why we have communicated that we expect more improvement across all business areas. Because we are moving into, you can say, our PCs over the summer and we will -- are committed to not letting our customers down, and we will take the initiatives needed to ensure that that will not happen. So it will continue to impact until we have the new capacity going live in Q2 of '18 -- sorry, Q1 of '18.

Cees de Jong: OK, thank you, operator. That concludes the call for today.

Operator: Thank you.

Ladies and gentlemen, that does conclude our conference for today. Thank you all for participating. You may now disconnect.

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