Chr. Hansen Holding A/S

Moderator: Martin Riise
28 June 2018
9:00 a.m. GMT

Operator: This is conference # 1699217.

Operator: Thank you for standing by, and welcome to the presentation of Chr. Hansen's Results for Q3 2017/2018. 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.

You are also welcome to submit questions via the web or by clicking on the Q&A button on the webcast or 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.

And I would now like to hand the conference over to your speaker today, Mauricio Graber. Please go ahead.

Mauricio Graber: Thank you, operator. Good morning, everybody, and welcome to the call. My name is Mauricio Graber, and I'm the CEO of Chr. Hansen. With me on the call today is Søren Lonning, our CFO.

Before we get into the results call, I think it's appropriate that I give you a brief comment after my four – first few weeks as CEO of Chr. Hansen. As most of you know, I have joined Chr. Hansen on June 1, after spending the last 23 years of my career with Givaudan and the last 12 as President of the Flavor division, based in Switzerland.

I could not be more excited about joining a company with such a strong heritage, performance culture and promising future. This is also what attracted me to Chr. Hansen, to build on the current high-performance and accelerate our journey as the global bioscience leader that fully leverages its unique microbial platform.

In my first few weeks since coming to Chr. Hansen, have spent time getting to know a lot of our colleagues and learning more about our business. I have also been in visits to some of our key sites in the United States, Denmark and France. And very important for me, I visit one of our largest customer's manufacturing and innovation center to experience firsthand the unique customer engagement model and innovation of our company.

I can tell you how proud I was to see the Chr. Hansen model working with our customers and creating share value. In the coming months, I plan to visit our colleagues and some of our customers and partners in China and Brazil.

It's important for me in the call today to make it absolutely clear that I fully support the Nature's number one strategy and financial ambitions that are attached to it. And we will get back to that later in these presentations, but my support of the strategy comes because of three things. The strategy of leveraging the unique microbial platform is unique to Chr. Hansen.

It's differentiated from competition and it addresses the key market trends and opportunities. I have been impressed not only with the quality of the Nature's number one strategy but also with the passion of execution of our teams, as well as the caliber and engagement of our people. This strategy is supported by an impressive research and development team, as well as by our fermentation scale up and manufacturing knowledge.

I think this company and the technology platform that we have offers a unique profitable growth opportunity for the future as we build further on our core and strong market position.

Please turn to the next slide. As I mentioned in my introduction, I think Chr. Hansen has some unique competitive advantages. The first is the market position, defined both in terms of technology and market share. The support of research and development platform, we're investing more as far as we know than any of our competitors.

My full sessions with the R&D department demonstrate the strength of our innovation and commercialization pipeline that will continue to deliver product, process and cost innovation. And second, it's our customer-centric model. We have a very close relationship to our customers especially in the core dairy business.

We have an outstanding mapping of the dairy market, which allows us to identify conditions business opportunities and deploy resources prudently to create share value from those opportunities. And finally, we have the advantage in the scale of production in our fermentation capability.

We are also very fortunate that multiple megatrends in the world favor our natural and sustainable technologies. The growing number of humans on the planet puts pressure on resources, and sustainable solutions need to be found for a range of problems like reducing food waste, reducing the use of pesticides in plants and reducing the amount of antibiotics used in animal farming.

Our microbial technologies can help in all of those cases. Perhaps, we can even help to create healthier and cheaper solutions for treating certain diseases or conditions in humans.

And speaking about sustainability, I think it's fantastic that we have documented proof that the majority of our business, meaning 81 percent of our revenues, directly contribute to the UN sustainable development goals.

Our three lighthouses are examples of business opportunities that we're actively pursuing. We were – and we believe that each opportunity holds a potential to generate annual revenues of at least EUR 100 million per year.

The leadership team presented an update of our Nature's number one strategy at the Capital Markets Day in London. We also presented an update on the long-term financials targets on the 2021/'22. Those targets are: to grow our revenues 8 percent to 10 percent per year with an average 7 percent to 8 percent contribution from food costs and enzymes; to increase EBIT margin before special item and acquisitions to above 30 percent; and to deliver a CAGR of around 10 percent in free cash flow.

And we defined targets for two of the lighthouses, namely bioprotection and plant health. In bioprotection, which is all about prolonging the shelf life for dairy and other food products while also removing chemical pesticides, we can grow to over EUR 200 million per year by 2025. In Q3, we saw both a record number of project inflows, as well as a record number of project wins. These give me tangible confidence that our lighthouse is tracking to deliver on its promise.

B, on plant health, our new business on biological nematode control can grow to the EUR 100 million target per year also by 2025. Our growth continues to accelerate as we see the second – the two new problems that we launched last summer, go ahead of expectation and just customer feedback has been fantastic.

We are just at the beginning of this journey with much upside potential as we expand to grow new crops and new geographies with microbial solutions that can be applied both to soil or seeds.

I have to be clear that to reach this EUR 100 million target requires us to have success in Latin America and also in other regions where we're currently awaiting product registrations.

While we have not yet defined the financial target for the human microbiome as this area is still too far in the future for us to put a specific target yet, where we do have some excellent news to share after Q3, which I'm going to tell you about in the next slide. Please turn to the next slide.

I want to talk briefly about 6 points of our Nature number one strategy that are highlights from my perspective. First, to emphasize a little bit more bioprotection, which grew 25 percent in Q3 and is around 35 percent for the first 9 months, the first generation of this technology, which is mainly selling in the developed world, is the main driver of our growth.

And the second generation of the technology which has been developed for countries where the core chain is less reliable typically in emerging markets, is beginning to sell well, particularly in Latin America.

Second, I want to touch on capacity. In food cost and analysis, the new capacity in Copenhagen is fully operational, and we are seeing the margin benefits as we have expected them.

Third, growth markets. The focus on growth markets across the business continues, and we're strengthening our presence in a variety of markets. This includes for example more application labs and resources for Food Cultures & Enzymes.

In Health & Nutrition, we are expanding our sales coverage, especially in EMEA and APAC. And in Natural Colors, we also announced that we're going to expand and modernize one of our key development facilities in Europe.

Fourth, getting to the human microbiome. We have had two significant scientific developments in Q3 which I would like to emphasize. First, we entered into a partnership with Prota Therapeutics to test our LGG strain in Phase III clinical trials to potentially develop a treatment for peanut allergy.

Prota Therapeutics is pioneering a new form of oral immunotherapy treatment, which combines Chr. Hansen's LGG probiotic strain with targeted doses of peanut protein.

The treatment is designed to reprogram the immune system, response to peanut and eventually develop tolerance. People who are allergic to peanut can have life-threatening reactions, so this is indeed a promising potential treatment.

The second development is the exciting result from a Chr. Hansen-led clinical trial that demonstrate how ingesting carefully – a carefully selected probiotic strain can reduce certain side effects associated with the regular consumption of acetylicsalicylic acid which is the regular ingredient in aspirin. Regular ingestion of aspirin can be damaging for gastrointestinal health, and this is the damage we can hope to address.

More clinical trials are needed, and the commercial opportunities have not been yet been fully assessed. But very exciting developments as I mentioned, in Q3 for Microbiome.

Moving onto plant health, the two new products that we launch, Quartzo and Presence, are selling well, even a little bit ahead of our expectations. The products are biological nematode controlled products and have been launched at an opportune moment.

The Brazilian authorities have recently banned some of the chemicals, which our products may replace. Our products offer a natural solution with performance that is similar to chemicals.

In addition, we have extended our collaboration with FMC, which is our distribution partner in plant health. The extended agreement continues to leverage the resources and expertise for both companies, while allowing for more flexibility to also collaborate with new partners.

Finally, our work on Natural Colors. We continue to see strong interest from food companies to use Natural Colors particularly in new product launches.

Also, I should mention that we have our new Executive Vice President for Natural Colors, and (Claus Barom) will be joining us from the food ingredient company (CP Kelco) in Denmark. We look forward to welcoming him and joining us at the beginning of August.

With this introduction, I would like to give the word to Søren Lonning to take us through the financial highlights. Søren, please.

Søren Lonning: Thank you, Mauricio. Please turn to the next slide for the group results.

Our organic growth rates was 9 percent in the first 9 months but with the negative impact from currency it corresponded to a 3 percent increase in reported revenue ended at EUR 801 million. So adverse developments in currency had a negative 6 percent impact between organic growth and the reported euro growth, roughly as expected at the time of the Q2 announcement.

Overall, growth was in line with our expectations and many of the drivers from the first half of the year continued in Q3. We saw strong performance in food (purchased) and supported by bioprotection, whereas Health & Nutrition and Natural Colors grew at a lower level.

Volume and mix accounted for 7 percent of the growth with euro-based price increases of close to 2 percentage points accounting for the majority of the remainder.

The EBIT margins before special items was 27.5 percent up in the first 9 months compared to 27.9 percent during the same period last year.

Our margins are negatively impacted by currencies, and those have been almost a full percentage point higher if the currency, most importantly, the U.S. dollar, had remained on the level of last year. The underlying performance of our business continues to be solid, and we are beginning to see benefit from the new capacity in Copenhagen.

R&D expenditures amounted to EUR 60 million or 7.5 percent of sales compared with 7.0 percent last year. The increase was partly driven by strategic initiatives, including bioprotection and LGG, the currency also impact the relative spend as the majority of our spending is in euro, which has increased relative share to sales this year.

Profit for the period ended at EUR 158 million, on par with last year. And finally, the free cash flow before acquisitions and special items were EUR 75 million, which is below last year.

The key reason for the decline are the change (inaudible) export credit scheme and timing of net working capital in Q3, which impacted working capital negatively. And finally, we also had negative currency impacting our EBIT.

Please turn to the next slide. Organic growth in food (inaudible) enzymes was 12 percent with strong growth in cheese, fermented milk, enzymes and meat and very strong growth in bioprotection, as Mauricio just explained.

Organic growth in Health & Nutrition is 8 percent year-to-date, driven by animal health and plant health and with low growth in human health. We achieved the strongest growth in the emerging economies throughout 3 areas in Health & Nutrition.

Natural Colors has grown by 5 percent organically with 2 percent from volume and 3 percent from prices. The higher growth and pricing is a combination of price increases driven by raw material cost, which is passed onto customers, general price increases and euro-based pricing.

Please turn to the next slide. Looking at our regions, we have grown 8 percent organically in the largest region of Europe, Middle East and Africa with 3 percent – 45 percent of group revenue. The growth was driven by strong growth in Animal Health, enzymes and meat and solid growth in cheese and probiotics for fermented milk.

The growth in bioprotection continues to be very strong in this region, and as said before, it is almost exclusively driven by first-generation technology so far. We also absorbed a slight decrease in Human Health due to inventory reductions with the key customer and infant formula.

Organic growth in Q3 was 10 percent, effectively the same drivers that also with a strong contribution from pricing driven by the euro pricing model.

North America was represented 25 percent of revenues. Organic growth was 3 percent. We saw strong growth in cheese, probiotics for fermented milk, meat and Animal Health. And in North America, we also saw strong growth from bioprotection. And like EMEA, the growth is with the first generation.

As we have discussed before, our dietary supplements business on the Human Health has seen some volatility through the year, but we see signs of recovery and expect improvements when looking ahead. Meanwhile, the infant formula business in North America is growing strongly. Natural Colors revenue were on par with last year.

In Q3, organic growth was 2 percent. Food (inaudible) and enzymes grew solidly, Human Health was flat, but our animal business saw a decline. This was primarily caused by the dairy farmer segment in North America, which is facing headwinds due to low milk prices. Milk prices are expected to improve over the coming quarters, and that should also lead to an improvement for us.

Asia Pacific represents 17 percent of group revenues, grew 17 percent organically driven by strong growth in fermented milk in China, Human Health with both Biogen supplements and infant formula growing strongly, Animal Health and Natural Colors.

Enzymes showed good growth while revenues from cheese and probiotics for fermented milk declined slightly due to timing of orders. Organic growth in Q3 was 11 percent, and again, driven by many of the same drivers.

And finally, Latin America, which represent 13 percent of our sales, grew 17 percent organically, driven by strong growth in cheese, fermented milk, enzymes and plant health. Animal Health showed modest growth, while revenue from Natural Colors decreased slightly compared to last year.

In Q3, organic growth was 20 percent with similar growth drivers. Natural Colors decreased slightly compared to last year due to our focus on higher value customer segments.

Please turn to the next slide. In food (inaudible) and enzymes the 12 percent organic growth after the first 9 months was driven by 9 percent growth from volume and mix and 3 percent from prices.

Of the volume growth was primarily supported by strong development in cheese, fermented milk, enzymes and meat cultures as well as modest growth in probiotics. Bioprotective cultures deliver organic growth of approximately 35 percent year-to-date and around 25 percent in Q3.

In Q3, organic growth was 11 percent and the drivers in the business were basically the same but with the pricing element being 5 percent. Key reason for the higher contribution from pricing is the euro price mechanism in certain countries, whereby a declining currency can support a high organic growth for Chr. Hansen.

The EBIT margin for the first 9 months were 32.5 percent, which was 1.1 percentage point below last year. As a result of adverse currency impacts and unfavorable product mix and the sales of a property in Argentina in Q1 last year.

In Q3, the margin was 34.7 percent, which was 0.4 percentage point below last year. The decline was driven by currencies, however, partly offset by positive contribution from the new capacity in Copenhagen facilities, which has started to materialize and is tracking according to plan.

Let us turn to the next slide. Health & Nutrition has delivered 8 percent organic growth after the first 9 months, all from volume and mix. Strong growth in Animal Health and very strong growth in plant health were partly offset by low growth in Human Health.

As we have explained before, Health & Nutrition can be more volatile compared to Food Cultures & Enzymes due to a higher customer concentration and exposure to agricultural commodity prices.

In Q3, organic growth was 7 percent. The situation with customers inventory reduction in North America in dietary supplements is improving, and we expect this business will return to growth mode over the coming quarters.

Meanwhile, infant formula contributed suddenly to growth in most regions and plant health grew strongly in Latin America. Animal Health only grew slightly due to the mentioned softness in North America, primarily within the dairy segment, while growth in the other regions, where we are investing in improved sales coverage, were strong.

The EBIT margin year-to-date has improved by 1.7 percentage points to 29.2, driven by a positive mix in Human Health, reduced breadth, insourcing of entity products and the absence of royalty payments for LGG. This more than offset a sizable negative impact on the (inaudible) U.S. dollar.

In Q3, the EBIT margin improved by 2.5 percentage point to 30.8 percent, mainly driven by a positive product mix in Human Health and favorable timing of production cost, which was only partly offset by adverse currencies.

Please turn to the next slide. Natural Colors grew by 5 percent organically with 2 percent from volume and mix and 3 percent from prices. The price increases reflected both increased raw material prices and general price increases.

Current food stock is the largest driver in natural products and we generally see more growth in emerging markets and in the areas of prepared food and ice cream and confectionary.

In Q3, organic growth was 6 percent and both North America, EMEA and APAC grew well while Latin America declined. The decline in Latin America was due to our focus on higher value customer segments. The EBIT margin improved in Q3 to 14.4 percent, up 0.3 percentage points to last year, driven by higher prices and the profitability focus that I mentioned (inaudible).

Please turn to the next slide. Looking at the currency impact of the declining U.S. dollars compared to the euro, the total adverse impact for the first 9 months has been around minus 10 percent.

Q3 was slightly better than Q2, and in Q4, the impact on the U.S. dollar on our revenue is expected to be immaterial. As a rule of thumb, a 5 percent decline in the U.S. dollar will have a negative impact on our top line of around EUR 15 million and around half of that impact on our EBIT.

The impact from all currencies on revenue in Q3 was minus 7 percent, and year-to-date, this impact has been minus 6 percent. The other currencies that are most relevant are the Chinese, Brazilian and Australian currencies.

In terms of the EBIT margin, the currency impact was minus 0.8 percentage point in Q3 and minus 0.9 percentage point year-to-date. And this is primarily driven by the U.S. dollar.

Please turn to the next slide. This slide shows the change in free cash flow after 9 months. We have had a slight improvement on the operating profit which would have been much stronger if the U.S. dollar had not declined so much compared to the euro.

The second major development in the free cash flow gives a change in the regulation around the Danish export credit. This is the one-off impact and impacts our working capital negatively.

This is the most significant impact on working capital, however, our net working capital was also affected by timing, partly (inaudible) by our sales being more back-end loaded in the quarter compared to last year. These drivers mean that our free cash flow year-to-date is EUR 75 million compared to EUR 98 million the year before.

Please turn to the next slide. As we communicated in our Q2 reporting, we would assess, together with the Board of Directors, the possibility of declaring an extraordinary dividend as part of the Q3 report.

And given the performance and cash flow generation in the first 9 months an extraordinary dividend totaling EUR 105 million equal to DKK 5.94 per share will be paid out on July 3, 2018. This is consistent with our capital allocation priorities, which we also confirm that the Capital Market Day in April.

Our priorities are, firstly, to invest in the organic growth through investment and innovation and capacity. Secondly, to invest in broader acquisition within our core business, either by acquiring companies that have interesting technologies or that can increase our market presence in attractive markets.

Thirdly, we pay out an ordinary dividend of 40 percent to 60 percent of net profit and finally, we will distribute additional cash to shareholders through either extraordinary dividends or share buybacks, all while having a leverage, which is consistent with a solid investment-grade profile.

Please turn to the next page. Based on the solid performance after the first 9 months of the year, we are maintaining the guidance on all group parameters. This means that we still expect to see 8 percent to 10 percent organic growth and EBIT margin and free cash flow levels in line with last year.

And with this confirmation, please move to the next slide. Please take a moment, at your convenience, to read through the Safe Harbor statement, and with this, I will now pass the word back to Mauricio.

Mauricio Graber: Thank you, Søren. Please turn to the next page. This concludes our presentation for today.

Before we open up for the Q&A, I have a few final remarks to summarize our call. Nine months into the year, we are on track to deliver on the targets we have set out, 8 percent to 10 percent organic growth with stable margins and cash flows despite some hard currency headwinds.

Our strategy, Nature's number one, is the right strategy for Chr. Hansen to pursue. Our technology platform and market positions are unique, and we can build on these strong points.

Our sustainability profile speaks excellently into the long term megatrends that we are playing into. Eighty-one percent of our sales directly support the United Nations sustainability development goals. And finally, I look forward to meeting many of you in the months to come and share my excitement on the promising future of Chr. Hansen.

Operator, please open the line for questions.

Operator: Thank you. As a reminder, if you wish to ask questions please press star one on your telephone and wait for your name to be announced. And if you wish to cancel your request please press the hash key.

Thank you, and your first question comes from the line of Hans Gregersen. Please ask your question.

Hans Gregersen: Good morning, a couple of questions. If we look at your comments on growth being more back-end loaded, what is the reason for that? Is any structural changes going on? And secondly, looking towards your cash flow guidance, what do you expect in terms of net working capital release in Q4? That's the first question.

Second question, bioprotection, can you give us some further insights into growth patterns across geographies, as well as obligations? And then finally you mentioned milk prices declined in Q3. What is the reason, in your view, and why do you expect it to recover?

Mauricio Graber: Thank you, Hans. Let me try to address that. The key reason for the timing in – of net working capital and back-end loaded sales in Q3 related to the timing of number of invoicing days and the timing of Easter. So this is to a large extent we had compared to last year, we had a bit more invoicing days in April, and we are also didn't have the Easter.

It was more – it was only in April the year before. And when we have the days outstanding, which are close to 45 days, that means that whether the timing between March and April can actually influence the amount of dues that we have outstanding. So it's not a structural change to your point. It is more of a simple timing thing that impacted last year. So that's a key point.

And we also had a little bit of timing, we did mention that, a little bit of timing on our tables that was lower than normal at the end of the quarter. But there is nothing structurally changing to that point.

Hans Gregersen: Can I ask you just on your payables comments, is that relating to the quarter ending on a weekend as well or...

Søren Lonning: No, that's a minor part of it. But it's true that sometimes when we are (inaudible) at a weekend, it can delay some payments coming in, but the key driver is really related to timing between March and April (inaudible) this year. If you move on to your second question regarding net working capital release in Q4, we will not make specific comments as to the net working capital development in Q4.

But we do expect to see an improvement in line with the seasonality we have in the business. Bear in mind that we are building inventories for – we have high seasons across our businesses in Q3 and Q4, and we are building inventories for that.

That will come down. We are also of course doing our outflows to optimize our collection at the year-end. So we will have some drivers that will help us bring net working capital way down from where we see now.

So that will be an important driver in terms of delivering on the cash flow guidance that we are giving. To your question regarding bioprotection. It is really driven by all regions and it's also driven by our three key process that we have today. So it's fermented milk, it's meat and it's cheese. Fermented milk is the largest contributor, but all of these clusters are going well and it's going well in all regions.

In particular, we have seen very good progress in Latin America. And we are also, I mean generation 1 remains the key driver, but we have quite good traction also on project progression in generation 2. So that is also looking promising for the future, so we're already selling and started selling, but it's not the key contributor.

But the pipeline looks really good. And as just an example, just (inaudible) in Q3 for the entire bioprotection, we won 60 projects with customers. So it's a quite solid ratio to have given the size of the business today.

Hans Gregersen: Just you mentioned that you won 60 current projects. Just to put that into perspective, how many projects if I can say so have you won as of now?

Søren Lonning: We – of course, we – our model is we win a lot of projects to drive growth in our Food Cultures & Enzymes business in general, reflecting also the market, the customer needs and the fragmentation in the market. But relative, the 60 wins in 1 quarter on bioprotection relative to the size it has today, it's quite sizable.

So although, bioprotection as expected came down a bit in Q3 due to the annualization of some very large wins last year that happened, that we won sort of midyear last year, then when we look forward in terms of the activities, the pipeline and the wins we have, then it looks quite good. We've had more than 200 project wins so far year-to-date in bioprotection. That's a lot.

We've addressed your questions regarding the milk situation, we are seeing quite low milk prices in North America at the moment, and it's starting to impact the buying patterns of the dairy farmers. We also see in North America the prices on pork also being relatively low. So in general the price in North America are on the low side. And it's starting to play into that dynamic that we see over there.

We are expecting milk prices, that's the projection to come up a bit in North America over the coming quarters. So we do expect it to be more a blip than a structural change for a longer period of time.

And then I would also emphasize that what creates a little bit more uncertainty in North America also at the moment is of course also all the discussions regarding trade restrictions, U.S. export, quite a lot of all sorts of agricultural products into China.

And with the recent debate at the foreign politics on this topic, it creates a little bit more uncertainty in that trade lane also. Just to say we are seeing a little bit more headwind on the macro parts in Animal Health right now.

But what I mentioned is the need for replacing antibiotics and increasing the efficiency and asset corruption through healthy and natural means remains intact and solid (inaudible).

Operator: And your next question comes from the line of Ben Gorman.

Ben Gorman: Just a few from me. First of all, in terms of the margin impact, specifically on the culture and enzymes division, you talked about 100 basis points of FX impact from the margin from a group perspective. Is that in line with Cultures & Enzymes? And you talked in the previous quarters about the impact of negative mix from strong enzymes growth.

What – can you quantify still around half a percentage point? And then sort of what's the impact as well, sorry, just on the same question, from the leverage on the new capacity?

You talked about the margin impact from the (inaudible) capacity being in line with your expectations and you previously talked about 200 basis points of gain as this capacity is ramped up.

How much of that 200 basis points have you got already? Sorry, that's a long first question. And then second question is on the FX impact being bigger in food rather than health. Is that just a geographical mix and what is that (inaudible)?

Mauricio Graber: Thank you, Ben, for the questions. Let me try to address it. If we look to your first question regarding currency impact in Food Cultures & Enzymes, then the impact of almost 1 percentage point is slightly lower in Food Cultures & Enzymes than the average. And this is driven by the fact that the – it is the, how we say the sales that's more broadly anchored across all region whereas Health & Nutrition is quite – has a quite high share in North America.

So this means that Health & Nutrition have the largest exposure to the U.S. dollar. So when you look at year-to-date, it's – it's almost 1 percentage point, around 1 percentage point for the group. Then it's slightly lower than that. But it's still above the 0.5 point. So it's somewhere in between 0.5 point and 1 percentage point without being exacting this part here.

If you move to your second question and the first question was regarding the mix, and here, we actually had a slight positive effect in – of mix in Q3. But if you look at it year-to-date, it's slightly negative. It's less than 0.5-point now. But we are still seeing a slight negative impact from mix. And that is driven by the fact that enzymes and, in particular, some of our less profitable enzymes, as an example, lactase solutions, have grown very strongly.

So there's a high demand for taking and removing the lactose from milk. So that's a good thing but it has a slightly negative impact on the margins year-to-date. But it's clearly below 0.5-point.

Then you ask regarding the leverage of our capacity. And I would say if you look at it for the full year, then it's close to 0 because we started the ramp-up in the beginning of the year. We have started to fully depreciate on the equipment, the assets.

And that meant that on a year-to-date basis, that it's close to null. But what's important to note is in Q3 where you actually saw a positive effect from the production. The underlying scalability of utilizing this more capacity, that had a positive impact. So overall, we are starting to see the progress, but on a year-to-date basis, it is still close. But it promised well for the futures.

We are expecting that all the time guided that second half. That's where we would start to see some benefit from that and that is coming through. So if you look to the Q3 margin, very roughly speaking, you will have around 0.5-point negative from currency, a little more than 0.5-point. But around 0.5 point negative from currency. We have made some investments in this quarter also into (inaudible) strategic initiatives that adds also here.

And then you have the production, which gives almost half a point in positive contribution. And that (inaudible) adds up to the minus 0.4 that you see. And then your final question related to the FX impact in food, in Food Cultures versus the rest of the business, and what – important points to make here that in Food Cultures & Enzymes, the – here we have the largest euro pricing mechanism.

This is where we have been able to implement the euro-based pricing mechanism most because of our market position. And that gives – that adds to the currency when you look to top line between organic growth and euro growth. But if you look at it as a U.S. dollars exposure as I mentioned before which is the largest exposure we have, then actually Health & Nutrition had the largest because of the large share of revenue in North America.

And then you would see the natural color has the lowest exposure, it's close to flat because we are sourcing a lot of raw materials in here. So there are dynamics into it but the key reason on the top line, that is there euro-based pricing in Food Cultures & Enzymes.

Ben Gorman: Can I just follow up on one very quick one, in terms of the euro based pricing on (inaudible) enzymes can you quantify that? It's obviously very heavily sort of skewed versus history and is less volume growth. I'm just sort of wondering what the organic number might have been if you take out the euro-based pricing.

Søren Lonning: In the quarter, it's a sizable impact, so we reported 11 percent organic growth, of which 6 percent is volume and 5 percent is price. And here, the majority of the price is euro-based pricing.

So I'm not going to give you the exact number, but we are below 5 percent, but we are close, up in that range, right? So it's a quite sizable impact. It's driven a lot by Turkey, Russia, Brazil, Argentina, these economies where we see the currencies coming down the way we've been protected.

And bear in mind, there's a little bit more volatility in this mechanism, but it is a way of safeguarding that we don't have to go out and make price adjustments in the local economies reflecting the high inflation in these markets.

So it's real – replaces some price increases we would otherwise have to go out and manually discuss her having said in an update discussed in customers we just build more automation in it. And that means that there can be more changes in that. On the full year, we have 3 percent from price increase, and here again the majority is the euro-based pricing.

Operator: And your next question comes from the line of Fulvio Cazzol.

Fulvio Cazzol: I have two. The first one is on Food Cultures & Enzymes. I noted that that the volume/mix growth within this division of 6 percent is the lowest that we have ever seen since we started to disclose I think in 2016.

I know that 1 quarter doesn't make a trend, but how should we think about the growth going forward? Is this a more realistic level versus the 8 percent to 10 percent that we have seen over the past 2 years?

And I understand the whole sort of mix impact from the lactose enzyme growth and the slowing growth within bioprotection, but just wanted to hear your thoughts on how we should think about that particular line going forward. And then my other question was for Natural Colors.

I was under the impression that you'd be refocusing more on top line growth as opposed to margins, but that doesn't seem to have gone through in this latest quarter. So how should we think about that strategy for that particular division going forward? Is that still the plan or is the focus more on profitability perhaps than we would have imagined since your Capital Markets Day?

Søren Lonning: OK, let me take your first questions, answer the first question. On Food Cultures & Enzymes, we are, as you may remember from our Capital Market Day, we are guiding 7 percent to 8 percent organic growth in this area.

And, if you remember, our growth driver model, then pricing, we expect to be around 1 percentage point. So according to our long-term growth ambition for this business area, then we would expect subsequently 6 percent to 7 percent volume growth going forward.

So that's our long-term guidance towards '22. Now we've been part – and there is no changes to that part. Now we have had some quarters now with very strong volume growth. And some of them have been supported by factors like bioprotection that will continue also going forward.

But we've also have some tailwind from China had grown at an abnormally high level from some years and that is normalizing a bit more now also given the high market share that we have in the market.

And we are seeing also – I mean we saw very high milk productions some years ago, we have a lot of milk flowing into cheese and that is also at the more normal level now. So I think we are maintaining our long-term guidance and based on that, volume growth of around 6 percent to 7 percent.

That's what that entails. If you look to your comment or question regarding Natural Color, I would say that we are not changing our strategy or plans here.

We are constantly trying to fine-tune the balance between sales growth and getting the right profitability. You're also absolutely right that we were looking into whether we had taken (inaudible) stand on this, and we continue to monitor that.

We have at this point in time not, how do you say it, we have not brought in, in Latin America Natural Colors, this, particularly Latin America, this is a topic for us.

We have not seen an effect of the adjustments that we have made at this point in time, but we are constantly checking that balance and really we have to deliver on both. We can't live with not seeing a top line growth.

Of course at the same time, we also want to deliver an attractive multiple – profit margin in this business. So not a lot of effect yet on the initiatives, but we are constantly balancing this.

What I would like to emphasize is that we did see a pick up in momentum in Natural Colors. We did grow 6 percent in this quarter relative to the 4 percent in the first half. So we are starting to see a little bit more traction in the color area, which we are of course pleased about.

Mauricio Graber: And Søren, I would like to add that we also not make any change on the direction of the color business. The rate of what I would call profitable growth will vary as well with the raw material trends and sometimes when we have increases in raw materials, we'll reflect those in pricing, and you may see the pricing component.

But overall, the transformation of our natural projects – of our Natural Colors division is about driving to best-in-class growth and leading our EBIT to the midteens as we have indicated.

Operator: And your next question comes from the line of Arthur Reeves.

Arthur Reeves: My question is about Animal Health in North America. You say that the sales have slowed down because of the pressure that dairy farmers are there under.

We did talk about this at the Capital Markets Day. Is there enough margin in that business with prices that farmers can afford for you to get the growth that you're looking for, for Animal Health, please?

Søren Lonning: I think there is. We're convinced there is. And I would also say, if we look at it internally, it is an area where we have quite attractive gross margins that are above the group average. So we, it's not an area you can say from a Chr. Hansen perspective where we have any reasons to not be pleased about the margin that we get out of it.

But I think we need to – we have to admit that in this business, we will see a bit more volatility, both from drivers, macro drivers and commodity prices, et cetera, but also from the fact that farmers and the veterinarians, they will constantly try out new products, and we need to be out there proving and convincing that our products are the best in the market.

So that's another dynamic that will also create a little bit more how do say fundamental volatility in the business than what we have in Food Cultures & Enzymes, where we had very little attrition when we – and we are selling there. So I think there's nothing here we – in what we are seeing right now, that we – that is very abnormal and not something we can't handle.

I don't think it means that – for sure it doesn't mean that the margin that we can command at the price point that we are selling in the market would make it anything but attractive.

Mauricio Graber: I think, Søren, that's a very good point. I may add that we personally met some farmers in the U.S. last month, and you see a strong conviction that better nutrition leads to better yield and performance for them.

So I think our products will definitely command the margin entitlement that we expect and it's more about a little bit the volatility that Søren talked about what they can afford as they work with their nutritionist on the best solution for their animals.

Operator: And your next question comes from the line of (Jonas Card Park).

(Jonas Card Park): Two questions from my side. First regarding the North American dietary supplement market, you're talking about bottoming out here in Q3, I'm also talking about category growing solidly. Could you maybe put some numbers on these trends to kind of build your case here?

And then just a clarification on the bioprotection, as you say, it grew around 35 percent year-to-date and 25 percent in Q3. You are also guiding towards a lower growth in Q4. Is it lower than the 25 percent or lower than the 35 percent?

Søren Lonning: If I take your last question first, I mean we are not guiding specifically on this segment here, but we are – what we are trying to say is that we had an extraordinarily strong first half of the year and that means our year-to-date growth rate of 35 percent, given that we have had this 1-year anniversary of some very large wins, that means that we expect less than the 35 percent also in Q4 and for the second half.

But otherwise, I will not give you specific guidance to this level here. And as I said, the activity level, the number of wins that we are seeing, we are seeing no reason why we shouldn't continue to report firm growth in the area.

Then if we look to the North American dietary supplement market, then I think it's important to say that the market has been – dietary supplements with probiotic have continued as a category for growth throughout this period here.

The two factors that have impacted us is, first, that there's been more players coming in and more players coming in without the trying to sell the products at – in a different way, claiming the number of bacteria as opposed to the quality and the impact of the bacteria. And that has created some confusion in the market. And secondly, there's been a move from the physical sales channels to the online sales channels. And that have also had an impact.

So that dynamic is still holding true, but the key customers that we're serving, remember we are working through partners here, they have been traditionally very strong in the physical retail part. They are building strength in the online, and you will see several of the players.

You will find also on the top-selling brands in Amazon. So they're getting better and better all the time. So they are also growing in their end markets. So the market is more challenging, but it is growing.

The thing that have hit us very hard this year is a customer of that, that built a lot of inventory, which brought that down and that's significantly impacted this year here. And that is the reason why we are in negative territory for this year. That being said, that's a temporary affect, and we do expect when you're closing this year to be back in solid growth in North America dietary supplements.

(Jonas Card Park): OK, so just to understand fully, this one customer, is the inventory adjustment done there or will there also be a negative impact in Q4?

Søren Lonning: It's – the majority of it is done. And we – there will also be a negative impact in Q4, but to a smaller extent. But what – we get 12-month forecast from several of our customers here, and here, we can see that these support, and I so probably when we start into financial year '19.

Operator: And your next question comes from the line of Heidi Vesterinen.

Heidi Vesterinen: So a couple, please. So on margins, you're guiding to flat year-on-year, and I think a few quarters ago, you had said that this guidance applies to all three divisions.

Are you still happy with this assumption? And then secondly, just to clarify on Animal Health in North America, so are you already seeing a recovery in that business or are you hoping or assuming that it will come back because you think the milk price forecast that are out there in the market are suggesting that the commodity prices would come back?

And then lastly, on Colors, I think previously we have talked a bit about some customers shifting back into synthetic colors, especially in the emerging markets. Is this something that you are currently seeing?

Søren Lonning: Yes, let me try to answer your questions and Mauricio can chip in. But at the Capital Market Day, we removed the guidance on the divisional level for

EBIT, so it's not part of our guidance anymore for those regions. What I would say is that we have said around – earlier for the year and it is also directionally correct.

We have seen – I think if we look at Health & Nutrition, that will definitely pull more, and we'll see a nice improvement here. We will also, when it comes to Food Cultures & Enzymes from Natural Colors, we expect to see some good (progress) in Q4, but we will not – it's not on the digit that we'll hit the level of last year, but we expect to see improvement in those two areas, also in Q4. And that's driven by when you look to food supplements.

As we continue to expect some participate momentum with the Copenhagen expansion and Natural Colors, the profitability initiative continues to impact positively. And then in addition, one of the things that's been killing us so far this year has been the massive effect on the U.S. dollar. As we discussed earlier on the call, that will be very limited based on the latest outlook on currency. So all that will help impact margins across our businesses.

So to answer your question, we will see more that we will see margin EBIT expansion in Health & Nutrition, and we guide on that also means that some of the others will not fully be on par with last year, but we do expect to see improvements in both of these areas in Q4. Then you have a question regarding Natural Colors and whether we are seeing the reversal to synthetic color as a dominant trend. That's not the case.

We have seen it in certain markets in a few incidents, but it's not a trend that we see happened in a very strong fashion and in a very broad geography context. So that's not the case, although, there has been individual examples of that. And then you had a second question regarding...

Mauricio Graber: I'll just comment a little bit, Søren, on the Color, which is, Heidi, as I mentioned in my remarks, what you see is consumer demand for Naturals is continuing at the very high level. How the customers are responding to that, I would say mostly by all of the new launches being with Natural Colors.

The conversions continue, and it has been just a very few selected categories, cereal as an example where they have been some shift back to artificial or keeping the natural and the artificial. But overall, the trend continues toward the conversion and the launch of Natural Color products.

Søren Lonning: And then you had a question, regarding, Heidi, animal health and the milk and what the impact would be for maybe the longer-term growth assessment of this business. And we don't see these things changing our long-term ambition for the position of being plus 10 percent. We are not guiding specifically for '19 at this point in time and we're not going to do it here either.

But we are seeing – we expect to see some improvement in this over the coming quarters in North America, and we also expect outside of North America. Remember, this is where we invest in building a stronger sales and technical support presence. Here, we expect to see continued strong growth in the coming quarters.

So we do expect Animal Health to improve in Q4, and we also expect that the fluctuation in milk and pork prices that we see right now is also more – is something that we also recall and will create better foundation in North America. So it's not changing our long-term guidance, and we expect to come back over the coming quarters. And then I think we have time for one more question.

Operator: And the next question comes from the line of James Targett.

James Targett: Just two final one from me, then. Just a couple – want to follow up on also check out a couple of the areas where you did say sales declined in the third quarter, which you haven't talked about, which is, and I guess cheese in APAC, Human Health in EMEA, and I think Natural Colors in North America, Latin America.

Just in terms of what – where you see the trajectory for those three particular areas over the next couple of quarters. And then secondly, maybe a question for Mauricio, just you view on Chr. Hansen's portfolio, a few of your, I guess, the wider peers have been moving into more adjacent categories to sort of increase their offering to customers, including I guess where you come from.

So I just wonder what your thought about the Chr. Hansen's much more narrowed focus and whether you think there is room for broadening out the scope a little bit.

Mauricio Graber: Then maybe let me address your first question, James. If you look to the areas of the sales decline, then in cheese, APAC, do bear in mind that it's quite a small market and a very large part of that is in Australia and New Zealand because there's a relatively low cheese consumption in Asia in general.

So this very much the weakness here very much relate to Australia and we have seen milk production coming down in Australia, and that's a general trend simply because of the changing climate conditions also as 1 element. So don't read too much into it. It's a 1 country and it's a relatively small segment in Asia Pacific. And it's not having a large impact on our overall cheese growth.

That being said, Australia is challenging at the moment because of the lower milk production generally. That also flows into cheese.

Your second point was related to Human Health in EMEA, and here, maybe two points: one is that we have some decline right now due to a few very specific customer events. One was a customer who made a large launch last year, and there are some, how do we say it, some timing of that also in the inventory, which impacts our sales negatively this year.

And another one, there's been some merchant activity also, which creates a little bit of defocus with one of our customers on this, so we're very much into the detail there are some specific customer things right now, that is impacting us.

That being said, Human Health in EMEA is an area that – where we expect growth going forward, but it's also the area where we have the relatively high maturation in some of the market that we're serving.

So it's not the high growth market of Human Health that will be more North America, (it’s been there) for a while and continue to see growth here. But it's emerging markets that will be very important growth driver also going forward here.

And then we had a last question, and I'm – I will take that on. I think the last question was, James, about some of the Chr. Hansen portfolio and my early read into thought, and great question, thank you for that.

So I would say there's probably very few companies in the world that have growth opportunity of 8 percent to 10 percent and improving margins. And I think that's one of the things that makes Chr. Hansen so unique. And coming up out of the equity years, the focused execution of this platform and the Nature's number one strategy I think is a very strong pillar for us to continue to be focused on.

So the way I see the portfolio of Chr. Hansen today is we have a very strong base in Food Cultures & Enzymes, our growth engines in Health & Nutrition and at Colors. So three legs for a company performing very strongly. And when I see the execution at the customer level, we bring a lot of value by selling – take dairy example.

Food Cultures & Enzymes into a dairy product, where we are now adding bioprotection and we can add probiotics. So I think the portfolio is very strong in our best direction we'll continue to be as a focused company, executing strongly against Nature's number one strategy.

Thank you, and that concluded the Q&A session.

Søren Lonning: Thank you, everybody, for joining.

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

END