Chr. Hansen Holding A/S
Q3 2018/19 Results
Conference Call Transcript

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10:00 a.m. CET

Operator: Good morning, ladies and gentlemen, thank you for standing by, and welcome to the presentation of Christian Hansen results for quarter three 2018 and '19.

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 and number one on your telephone.

I must advise you that this conference is being recorded. I would now like to hand the conference over to your speaker today, Christian Hansen's CEO, Mauricio Graber. Thank you.

Mauricio Graber: Good morning, ladies and gentlemen and many thanks for joining Christian Hansen investors and analyst call on the early release of our Q3 2018/2019 results.

We acknowledge that this call has been set up on a short notice and appreciate your flexibility in dialing in today. But it was important for us to provide you with a full explanation for the changes to our top line guidance now and not in a week's time.

As usual, I am here with CFO, Soren Westh Lonning, and we will do a short presentation on the business developments of the last quarter and comment on the new guidance for you before we move into Q&A. Please take notice of the safe harbor statement on Slide 2 before we continue. Thank you. Let's turn to Slide 3.

During the last three months, we faced more challenging trading conditions than anticipated, and whilst I see (inaudible) disappointed that in specifics part of the business and regions we did not manage to live up to our own expectations, and therefore, needed to change our growth guidance for the full year.

But let me start by saying the following – despite headwinds, Christian Hansen delivered a solid organic growth of 9 percent for the first nine months of our financial year 2018/19 and increased EBIT margins before special items of 28.2 percent , and there are very few companies in our sector that can deliver this.

In Q3, we also made good progress on profitability with a strong contribution from our Copenhagen site expansion. But sales momentum was lower than anticipated, leading to 8 percent organic growth for the group, a solid result but below our expectations.

The reasons were threefold. Despite strong efforts of the entire team, we were not immune against some of the more challenging economic climate in emerging markets, which hit Natural Colors relatively more than the other two segments.

Secondly, for the first time in over a decade, our Food Cultures & Enzymes business has experienced negative growth in China, driven by relative maturity of the fermented (bean) market and more challenging customer dynamics. And thirdly, we also have not seen a recovery in our Animal Health business to the extent that we expected.

Free cash flow before special items and acquisitions came in at EUR 57 million year-to-date, lower than last year due to higher investment activities, but this is in line with our communicated expansion program as we continue to invest in our strategic priorities.

Let's turn to the next slide, 4, so that we look at the sales contribution of our three segments look like for Q3 and year-to-date. First in Food Cultures & Enzymes, organic growth came in at 9 percent year-to-date and 8 percent for Q3, driven by both volume and price.

Cheese, meat and enzymes delivered strong growth, and I am pleased to also see and report that we have seen momentum improve in our bioprotection lighthouse increasing, again. Both our fresh dairy business, with fermented milk and probiotics was challenged, particularly in Asia Pacific.

In Health & Nutrition, the business accelerated compared to Q2 leading to double-digit organic growth rate of 11 percent in Q3 and year-to-date. Plant Health reported particularly strong results, and we also saw strong contribution from infant formula. But Animal Health did improve (but) slightly – improved farmer economics in the U.S. and new customer wins but, clearly, not to the extent we had expected.

Lastly, in Natural Colors, we saw another deceleration in organic growth to 3 percent in Q3, driven by declining raw material prices and slower momentum in emerging markets, particularly Latin America and the Middle East leading to 4 percent growth year-to-date.

Please turn to Slide 5. Regionally, growth in North America picked up in the third quarter, while we saw softer momentum in EMEA and APAC. Europe, Middle East and Africa delivered solid growth of 7 percent year-to-date but only 4 percent in Q3, and this was driven by flatter sales in Natural Colors, mainly due to lower demand in the Middle East and declines in Health & Nutrition. For the latter, timing in orders with a major customer in Human Health was the key reasons.

Very positively on the other side, in North America we have seen steady improvement over the past three quarters resulting in 9 percent organic growth for Q3 and 6 percent year-to-date. The performance in Q3 in North America was driven by both strong results in Food Cultures & Enzymes and Natural Colors, as well as increased momentum in Health & Nutrition, although Animal Health did not perform as strong as expected and the dietary supplement market was still subdued.

Turning to Asia Pacific, overall, we've seen better performance during the past three months compared to the last quarter, reporting 3 percent organic growth for Q3 and 4 percent year-to-date but it's still clearly below historical levels.

Health & Nutrition reported strong growth, while Natural Colors declined due to softer demand and timing of orders, and Food Cultures & Enzymes declined mainly due to the already mentioned slowdown in fermented milk growth and customer dynamics in China.

Lastly, in Latin America, organic growth came in at 27 percent in Q3 and year-to-date with unchanged dynamic compared to the first half of the year. Food Cultures & Enzymes and Health & Nutrition delivered strong growth, while Natural Colors faced headwinds from raw materials, challenging economic conditions and competition in commodity pigments. Euro pricing accounted for less than half of the organic growth in Q3 and year-to-date.

With this, I would like to hand over to Soren for a detail of our business segments and group financials and our new guidance for the year.

Soren Lonning: Thank you, Mauricio, and good morning also from my side. Food Cultures & Enzymes delivered solid organic growth of 8 percent in Q3 and 9 percent year-to-date driven by strong momentum in cheese, enzymes and meat as well as bioprotection growing approximately 15 percent organically. Momentum in fermented milk was lower in Q3 as already explained by Mauricio, leading to a solid growth year-to-date.

Probiotic sales declined in Q3, except for North America where we continue to see solid growth also from cross-selling with our plant-based cultures, overall resulting in a slight sales growth year-to-date for probiotics.

The contribution from euro pricing was three percentage points, so a little lower than from the first half of the year and in line with our previous comments that the positive impact would decline over the course of the year.

Looking at profitability. The EBIT margin for Food Cultures & Enzymes increased by 40 basis points in Q3 and 50 basis points year-to-date driven by scalability benefits from increased capacity utilization at our Copenhagen site, which were partly offset by investments in Nature's No. 1 initiatives, such as digital as well as additional sales and education resources for areas like bioprotection or fermented beverages.

With regards to the gross margin improvement from the Copenhagen expansion, please remember that we saw first benefits materialize already last year in Q3. Overall, we are halfway through reaching the 200 basis points that we guided for and the remainder will come at a slightly lower pace over the next two financial years. Please turn to the next page, Page 7.

Health & Nutrition accelerated in Q3 leading to 11 percent organic growth for the quarter and year-to-date. Human Health delivered solid growth in Q3 driven by a continued strong growth in infant formula across all regions, while (Theracheck) dietary supplements was on par with last year, once again affected by the subdued dietary supplements market in the U.S.

Animal Health momentum improved compared to the first half of the year leading to solid growth for Q3 and good growth year-to-date with a strong contribution from swine and poultry. However, better momentum in capital did only partly materialize as new customer wins and somewhat improved farmer economics towards the end of Q3 were not enough to have a material impact.

Lastly, if we look at Plant Health, we are really pleased about the continued uptake in Brazilian sugar cane leading to another quarter of strong growth and this despite a high comparable. Furthermore, I am happy to report that in Brazil, we are increasingly expanding into soy, whilst doing trials with customers in other crops and countries. That said, please do not forget that Plant Health is still a small business for us, which by the end of the financial year, will account for about 5 percent to 10 percent of Health & Nutrition.

If you look at the margin development for Health & Nutrition, the EBIT margin in Q3 and year-to-date was on par with last year. With regards to last quarter dynamics, lower gross margin due to unfavorable product mix was offset by relatively lower growth in other expenses relative to the top line.

Let's continue with Natural Colors on the next slide, Slide 8. As already outlined by Mauricio, organic growth in Natural Colors decelerated to 3 percent in Q3 and 4 percent year-to-date.
Whilst we continue to see strong growth in one of the key premium segments, (inaudible), this was not enough to offset declining sales in certain traditional natural color segments.

Most notably, we saw the impact from declining raw material prices and challenging economic climate in Latin America and Middle East, whilst APAC declined, not only due to softer demand but also because of timing of orders. Please note that Latin America was particularly impacted because here, we had a higher exposure to raw materials like (natural) and carmine, which declined.

Whilst I'm clearly not fine with the performance of Natural Colors, let me also say that the slower top line did not have a negative impact on Natural Colors absolute EBIT contribution. The business was also able to protect and even expand the margin by 1.1 percentage points in Q3 and by 1.6 percentage point year-to-date. In Q3, the margin expansion was driven by operating efficiencies as well as declining raw materials.

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Moving on to the group financials on the next page, Page 9. Group organic growth came in at 9 percent year-to-date with a volume component of 6 percent and a 3 percent contribution from price. The impact from currencies on the top line was minus two percentage point, whilst the (inaudible) acquisition did not have a material effect.

Please note that for Q3, Q4, we expect a positive currency impact of around one percent. If we look at the P&L, gross margin improved by 1.5 percentage points year-to-date driven by all three businesses, but mainly Food Cultures & Enzymes and Natural Colors whilst operating expenses increased by 0.8 percentage point to 27.2 percentage points revenue due to Nature's No. 1 investments.

Overall this led to an EBIT margin before special items of 28.2 percent for the first nine months of the year, up 70 basis points. In Q3, the EBIT margin before special items was 30.4 percent compared to 29.7 percent last year. The impact from currencies was immaterial.

Lastly, primarily in connection with the (Hundsbichler) acquisition, we booked special items of EUR 1 million resulting in an EBIT margin of 28.1 year-to-date and 30.2 in Q3. For the full year, we expect special items of around EUR three million related to both (Hundsbichler) and the joint venture with Lonza.

Please turn to the next page, Slide 10, for the cash flow analysis. Free cash flow before special items and acquisition came in at EUR 57 million, EUR 90 million lower than last year mainly driven by increased investing activities.

Operating cash flow increased by 3 percent with growth in operating profit and a favorable impact from higher non-trade payables related to the discontinued export credit scheme last year, which were largely offset by higher taxes paid due to the (absence) of acquisition-related tax benefits. Operational investing cash flow was 11.3 percent of revenue compared to 9.1 last year, and this is in line with our expectations.

However, given that we have decided to postpone some of our investments into the next year, the total CapEx won't be lower than previously indicated, EUR 110 million to EUR 130 million net of sale and leaseback. The sale and leaseback process is progressing as planned and we continue to expect the cash inflow in Q4.

Coming to the guidance on the next page, Page 11. As Mauricio has already elaborated, the slower sales momentum in Q3 and the outlook for the remaining quarter means that we have taken the decision to downgrade the organic growth outlook for the full year as follows – we now expect organic growth of the group of 7 percent to 8 percent.

For Food Cultures & Enzymes, we continue to expect organic growth to come in above the long-term ambition of 7 to 8 percent with euro pricing being the main driver of the higher growth. For Health & Nutrition, we now expect organic growth to come in around 10 percent compared to 10 percent or above before, as we have lowered our expectations for Animal Health.

And lastly, in Natural Colors, we downgrade to 4 percent to 5 percent organic growth from previously 5 to 7, in light of the declining raw material prices and softer momentum in emerging markets.

Naturally, our outlook is based on what we know today about the state of our business and the broad economic picture, but we have also stated throughout this financial year that events like a hard Brexit, increasing trade tensions between major economies, plus further worsening of the climate in the Middle East and in emerging markets more broadly can have a negative impact on our business.

The implied guidance for our organic growth in Q4 covers a fairly wide range. Let me just be clear, the scenario of the group growing at organically at 7 percent for the year is a scenario that includes basically all downsizes that we have identified and realizing none of the upsides, and this is clearly not what we're aiming for.

Looking at profitability. The EBIT margin before special items is still expected to be around 29.5 percent supported by scalability benefits from the expansion in our Copenhagen facility and the gross margin improvement in Natural Colors, which will partly be offset by investments into our lighthouses and other Nature’s No. 1 initiatives.

Lastly, free cash flow before acquisition, divestments and special items is now expected to be higher than last year due to the previously mentioned postponement of selected CapEx projects, while the proceeds from the sale and leaseback are still expected for Q4.

In terms of capital allocation, and please turn to slide number 12, we will continue to provide value for our shareholders by investing into capacity, innovation and people for organic growth, our number one priority, whist also keeping an eye out for suitable acquisition target to expand our market presence and technology platform mainly within Health & Nutrition and Food Cultures & Enzymes.

We also remain committed to paying our shareholders an ordinary dividend of 40 percent to 60 percent of net income and we'll distribute additional cash in form of extraordinary dividends and share buybacks in absence of large M&A.

Based on the cash generation during the first nine months of the financial year 2018, '19, management, together with the Board of Directors, has decided to distribute an extraordinary dividend of EUR 110 million, or DKK 6.24 per share, which will be paid out on July 8th.

And with this, I would like to hand back to Mauricio.

Mauricio Graber: Thank you, Soren. After we have gone through the financials of our (three) segments and our (foreign) regions in depth, and before we wrap up and open the floor for questions, I would like to put the quarter numbers into perspective and refer back to our Nature’s No. 1 strategy.

I know that quarterly results are important, particularly when expectations are high and it's on to us to deliver quarter-after-quarter. But let me emphasize that neither slower growth in Chinese yogurt market, that does not come as a surprise; nor the temporary headwinds in emerging markets, declining raw material prices or weak farmer economics, changed the mix to long-term opportunities for Christian Hansen.

We remain committed and confident on our long-term financial ambitions of 8 percent to 10 percent organic growth, 7 percent to 8 percent for Food Cultures & Enzymes and increased margins to our EBIT, 30 percent loss margin. With our Nature's No. 1 strategy, we are exceptionally well positioned to further leverage the power of good bacteria and develop products and solutions for the food, agricultural, nutritional and pharmaceutical industries that will deliver strong organic growth for shareholders and value for society.

Nature's No. 1 is all about leveraging the food potential of Food Cultures & Enzymes, further developing our microbial platform for human, animal and plants in Health & Nutrition and delivering value-creation in Natural Colors through innovation, growth market as well as operational efficiencies. We continue to be very focused on execution and made good progress over the past nine months on advancing the strategic priorities set for this year.

In Food Cultures & Enzymes, we launched several new products, including culture solutions for dairy alternatives, a rapid growing market niche; and sugar reduction as well as our strategically important CHY-MAX SUPREME cheese (coagulant). All those examples are proof of our innovation power and important drivers for our Food Cultures & Enzymes growth in the near to midterm.

We are also making progress with our bioprotection lighthouse. As for today, we have about 500 customers and won more than 180 projects over the last 12 months. We're confident in the 200 million lighthouse target.

And I strongly believe in our ability to increase adoption of bioprotective cultures, not only in traditional fermented products, but also in adjacencies like salad, salmon and meat because it's a clever way to extend shelf life, reduce food waste or take out chemical preservatives with nature's own sources.

In Health & Nutrition, our human microbiome lighthouse, the joint venture with Lonza, is awaiting merger control clearance to pave the way for bacteria-based pharmaceuticals, a market which is rapidly emerging and estimated to reach EUR 150 million to EUR 200 million by 2025. For a second lighthouse in Health & Nutrition, Plant Health, we are on track with launching our bionematicides, Quartzo and Presence, in the U.S. market this fall.

Lastly, in Natural Colors – while the overall trend towards natural solutions is unbroken and we have seen very good strong momentum with conversion wins in North America recently and continued solid growth from coloring foodstuffs, there is a key challenge that we need to overcome.

Absent regulation in markets like the U.S, we need to work even harder to bring better and more cost-competitive solutions to drive compared, particularly of legacy brands. This is a challenge because while brand owners are interested in converting to more natural ingredients, the costs typically go up when doing so.

To wrap up, let me be very clear, last quarter's performance fell short, not only of market expectations but also our own expectations even though we still delivered solid organic growth of 8 percent for the quarter and 9 percent year-to-date at improved profitability.

While we have adjusted our outlook for the year, it's also clear that reaching our long-term ambitions of 8 to 10 percent organic growth for the group, 7 to 8 percent for Food Cultures & Enzymes will not just fall into place but will require us to work hard every day on developing new products in R&D, driving scalability and operation efficiencies in production, and serving our customers the best way possible and convincing regulators of the benefits of biological solutions.

I have been CEO of Christian Hansen for a little over one year now and what I – it continues to be most impressed is the dedication and drive of our team. At Christian Hansen, we come to work every day to develop new solutions for less food waste, less pesticides and antibiotic use in farming and more efficient livestock production and bringing healthier products with less sugar, less artificial ingredients and cleaner labels to market.

I firmly believe that with Nature's No. 1, we have the right strategy in place. We have a strong purpose with our sustainability leadership, and we have the team onboard that is needed to deliver exceptional results going forward.

Thank you very much for listening, and we're happy to take your questions now. Operator, please go ahead and open the line for questions.

Operator: Thank you so much. For the question-and-answer session, participants are kindly asked to limit themselves to three questions only, and a final reminder, if you wish to ask a question, please press star and the number 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 Annette Lykke. Your line is open, please go ahead.

Annette Lykke: Thank you so much. My first question will be to your outlook for 2018/'19, 7 to 8 percent growth. If I'm right, this is an implicit growth of maybe 5 to 6 percent for Q4. Please elaborate on – on when – what areas you see the growth further down and in particular, I'm of course interested in how you see (inaudible) to perform also in markets like China?

Then, could you elaborate on your bioprotection, the EUR 200 million target by 2025, how do we set? What is the assumptions behind this? How much should come from any new indications? What will APAC contribute? And will they contribute to this target? And, how sort of certain do you feel?

And then my third question will be on the Chinese market. These structural changes, how soon do we see these to change? I think you have previously said that you believe that the more mature Chinese market will grow from innovations, but how long time will these innovations take to be implemented and then adopted in the market? Thank you so much.

Soren Westh Lonning: OK, Annette, let me address your first question regarding the FY '19 outlook and the areas for downsides and risks. It's clear that when we – the key risk areas that we are looking into is related also to the areas that we mentioned as disappointments for the Q3 performance and the reason for taking down the guidance.

So, that will be more broadly emerging markets, both Natural Colors in Latin America and Middle East, in particular, and also Food Cultures & Enzymes in China where we, at the moment, based on Q3, is a negative – negative territory.

And then when it comes to Animal Health, I mean, we're still working to improve the momentum in the Animal Health business. But again, here, it is an industry where the environment also plays a role in how fast we can drive commercial adoption in our solutions. So I point to those three risk areas.

In addition, let me just add that, in particular, Middle East is also an area that we are basically here assuming that we will remain more or less as it is now. But over the last months to two, we do believe – we have seen the Middle East deteriorating. So I think that's also a risk area to point out.

But I said earlier, when it comes to the Q4, the span that we have given, 7 percent to 8 percent is a pretty wide span for Q4, and that it reflects whether we sort of see all the risk that we are looking into materializing in the worst case or whether we, in the positive scenarios, are able to overcome several of these challenges and maintain a solid Q4 performance as well.

Annette Lykke: But do I understand you correct, Soren, that you actually anticipate a further decrease of growth in China for the (FCE) products?

Mauricio Graber: I think what we are working on is to turn the China situation around, so we will move into positive territory. Note that the baseline in China is also becoming slightly more favorable in Q4 relative to the development we saw last year. So that's – that is the plan.

But it comes, let me point out it comes with a risk to lift a momentum, of course. It requires us to be successful with customers and also change some of the customer dynamics that we alluded to before. So that's how I would (phrase) the China part.

Soren Westh Lonning: (Also) your question about bioprotection. Basically, we have seen a stronger growth in our Q3 coming back to 15 percent . I think we are – we have said in previous calls, we are breaking new ground with bioprotection, which is a different way for customers to use bioprotective cultures.

And we will continue to innovate. We have launched the second generation, we are working on the third generation and its expansion curve as we work in bioprotection. For sure, you can make the calculation of us having to grow bioprotection at roughly 20 percent to deliver on our EUR 200 million lighthouse.

But the amount of activity, customer engagement and interest in the category give us great confidence that we will continue to grow at the high double-digit growth and close the gap to achieve our EUR 200 million lighthouse.

Annette Lykke: Thank you so much.

Soren Westh Lonning: Anything else you might want to add?

Annette Lykke: No, that was it.

Mauricio Graber: Then your third question, Annette, related to China and the changes here. I mean, it's really split in two. We have seen the market for yogurt overall lowering the growth, so we are now in mid-single-digit territory in China as we see it. So that's a general trend that has been ongoing, and we don't foresee that to change.

But what the whole Christian Hansen model is that we are not only pleased with growing with the market growth but that we will also bring value-added solutions, bring additional benefits in addition to the (core), value-adds, and that is what we aim for also in terms of driving growth.

And so we're not just a (market) growth company. Now we're more specific as we mentioned here with customer dynamics. I mean, that relates a little bit how is the growth in China, volume versus price, what the customers want, winning, losing share in the market and also product mix with the customers that we are serving, which segment is it that are growing most at the moment.

So those are the elements that brings us from a market growth of around 5 percent into negative territory. And these are the ones where we are really working and turning it around in addition to bringing the value-add services that can lift us further above the market growth.

Soren Westh Lonning: And may be to add just a little bit of color to that, I would say overall, the consumer dynamics in China are challenging. If you put yourself – first of all, there's been a contraction in the economy. Swine prices are higher. So the disposable income or the basket for the customer is getting more expensive.

And the dairy category is still an aspiration rate category, whether it's ambient or chilled. So that's when we talk about an overall more challenging underlying economics in the market. Still what we bring to the market related to innovation and working with our customers to drive category growth is what gives us the confidence on let's say, within that more challenging environment, controlling our own destiny and finding avenues for growth.

I think this will take some quarters of us continuing to push and work with customers but confident I would say, the next wave of growth in China will be part of our future growth model in Food Cultures & Enzymes.

Annette Lykke: OK, thank you so much.

Operator: Thank you. And if you wish to cancel a request, just press the hash key. Your next question comes from the line of (Jonas Goldberg). Your line is open, please go ahead.

(Jonas Goldberg): Yes, thank you and good morning. I have a couple of questions here. First of all, on the decline in traditional Natural Colors pigment sales. Could you explain what is going on here and if it's structural decline or what it is, more specific? And then, a clarifying question on bioprotection. In Q3, are there any one-offs negatively impacting the organic growth of 15 percent or is it though to be clear organic growth? Yes, that was it, thank you.

Soren Westh Lonning: Yes. Let me address these questions, (Jonas). When we talk about the Natural Colors market, you would say that if you split the market in sort of the value adding similar to the food color and stuff, that is really what is driving most of the market growth. The more traditional pigments are growing, but at a lower pace.

And you can say, so there is a structural change between those two. They don't change the overall market growth, but it's just a balance between those two segments. And I mean, we are fortunate to be also exposed in the value-added part.

What we have seen also based on history in Christian Hansen is that after a period where raw material components have increased in price and is then coming down, we have seen – the picture that we are seeing now also with organic growth being lower in Natural Colors because the – of our price position on some of these traditional pigments as the raw material (inaudible) comes down. But then that is often combined with a quite strong development in EBIT.

We have seen this before, and this is also what we see here. So it’s – there is a structural change to your question where there's is definitely more higher growth in the value-add segments, but there is also growth in the other (segment). And the pattern that we're seeing now is not that unlike what we have seen following former price – major price changes in the color market.

(Jonas Goldberg): OK.

Soren Westh Lonning: When it comes to bioprotection, I would say that whether the 15 percentage (is clean), that is reasonable (clean), from the point of view that we are still impacted, to some extent, by these customers in North America, a key – a few key customers that we alluded to before. But that is moving towards a more normal state still as someone – some impact. But otherwise, I mean, we continue to see good traction on the pipeline with customers with interest in the products, et cetera.

And then just reflecting a little bit, I heard that some questions or comments regarding that the baseline is becoming easier in the second half of '19. Let me just say that the reason for – you can say that organic growth was lower in the second half of '18 and in the first half of '18, was more driven by the wins we had in '17 that annualized. So you cannot really deduct on the growth level in '18 whether the baseline is easier in '19 or not.

So I would say, we are getting closer to a more clean state, but we still have a negative impact from these few larger North American customers, which we discussed earlier.

(Jonas Goldberg): OK. Thank you very much.

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

Arthur Reeves: Good morning. Question from me, please, on visibility. I think you have good visibility in Food Cultures & Enzymes, but what can you do to improve the visibility in Animal Health and Natural Colors so that we don't get this sort of surprise, please?

And then my second question is, are we looking – I know you don't want to talk about next year, but are we looking (of) getting back in line with midterm guidance throughout next year, or do you think some of the trading conditions you're facing in fourth quarter '19 will carry on through into the first half of '20? Thank you.

Mauricio Graber: I'll address first, your last question and then Soren will comment on the Animal Health and Natural Colors visibility. We're clearly not now giving guidance for next year, but we'll do that whether – with our Q4 results. But I think I was clear during our conference call on expressing both our commitment and our confidence to our long-term financial ambitions, so 8 to 10 percent at improving margin.

For sure, if trading conditions continue to be challenging, we may be in the lower end of that range, but the innovation and growth opportunities that we view for our microbial platform and our natural solutions, I think definitely entitle us to remain committed to – to that range.

Soren Westh Lonning: Yes, and to your first question, Arthur, regarding visibility, I mean, there's basically nothing we would rather have than increasing our visibility in those category. But it is more challenging for various reason. The farmer market is quite dynamic and varies by segment, so it's difficult to structurally remove that.

You can say the more that we can – that we can make probiotic what is considered an essential in the diet of livestock animals across segments will reduce the – you can say the fluctuations that we see, as long as it's considered still a nonessential, it is something where farmers are considering all the choice of whether or not to include in the diet. So I think that's (a core thing) that we can work on.

In terms of the Natural Colors, what we really can do here is to continue to deliver, convert more and more of our business into value-added solutions that have a higher degree of differentiation and then makes it more difficult for our customers to swap between us and a competitor, because that is really what is the difficult part to fully predict.

So I think on both of them, it's something that we will work on, and that's part of our strategy but it's also something that is not likely to change within the next 12 months in a way where we will materially change the visibility we have in those businesses.

Mauricio Graber: But the trends, I would say overall the trends in Human Health, Plant Health and Animal Health are continuing to have increased interest in reduced use of pesticides and more use of biological solutions, increased use of the benefits of probiotics for Animal Health and Human Health.

So while you may see some more quarterly variations, I think overall, the annual progression of our Health & Nutrition division being a high-growth business area will continue to be there for us.

Arthur Reeves: Thank you.

Operator: We still have a question on the phone. It comes from the line of Soren Samsoe. Your line is open, please go ahead.

Soren Samsoe: Yes, hello gentlemen. First a question on your new guidance for this year, if you could just tell us how much you have assumed for – backed by euro based pricing in Q4? And also then if you could say going into next year at current spot rates, what kind of euro-based partings on organic growth would you expect? Would it be negative, would it be positive?

And then a question in – more in terms of your long-term guidance. If these sort of tougher market conditions in emerging markets and also how Natural Colors have developed and also Animal Health, is that a (step) to evaluate your long-term guidance? And then maybe consider using a broader range if you could you just elaborate on your thoughts there? Thank you.

Mauricio Graber: Let me address your first question, Soren. The guidance for the full year of 7 to 8 percent assumes a close – I mean, immaterial effect from euro-based pricing in Q4. And this is largely driven by the fact that of the changes that we saw last year where there was quite a lot of changes in the Argentina's peso and Turkish lira, et cetera, happening during our second half of the year. So it's primarily driven by that.

So close to zero impact in Q4, and that is also why we are guiding or we have mentioned that we expect a positive currency effect to the tune of roughly one percentage point in Q4, and that is primarily the U.S. dollar that we'll give that in the – in Q4.

When it comes to next year, you can say that the euro-based pricing – and bear in mind here that this is assuming that this – the current currency rates and based on experience – those can change a lot in the course of three to four months. But if you look and use the rates that is right now, it would be – it will again be immaterial, the effects from euro-based pricing next year, based on what we see right now. So that Q4 picture will continue into FY '20 based on existing rates.

I think on the long-term guidance, I don't have so much more to add than what Mauricio has already said. We are not, right now, considering to change our guidance. We believe that our technology platform, the consumer trends that we are tapping into provide us the opportunity to maintain our long-term guidance.

But also as Mauricio alluded to, the trading conditions being tougher right now may push us more over to the bottom end of that. But that is speculation at this point in time, because we have not gone through the exercise of really looking into how it would look also next year to the extent that we will be able to provide a guidance for (FY '20) at this point in time.

Soren Samsoe: No. It was more like that, not so much move the develop of the guidance, but more that you also said that you are seeing (higher uncertainties) in the market, so I thought it could be that it could be relevant to use a broader range. But, it doesn't seem like that?

Mauricio Graber: We will consider also following what has happened here in Q3, what would be the most appropriate way to guide when we get to (inaudible). So that is something we'll consider.

Soren Samsoe: OK, thank you.

Operator: And the your next question comes from the line of Heidi Vesterinen. Your line is open, please go ahead.

Heidi Vesterinen: So a few question, please. Could you update us on dietary supplements, please, because you seem to be losing share. What has gone wrong and how are you going to rectify this? And then secondly, in the parts of FC&E and H&N where you are seeing challenges, would you consider reducing prices to gain volume?

And then last question, maybe coming back to the guidance. I was surprised you decided to (inaudible) last night, because actually, the actual earnings (cut) is quite limited when you look at 2019 consensus, right, in terms of what you're implying? So is there an underlying message here that 2020 estimates are too high? Thank you, those are my three questions.

Mauricio Graber: So maybe Heidi, I will comment on dietary supplements and Food Cultures & Enzymes and then pass it on to Soren on the guidance.

So dietary supplements – first of all, I would say, the overall interest on probiotics as part of Human Health, I think continues to see a very positive trend and demand of using probiotics as a source of infant and growing up nutrition, adult nutrition, more probiotics being used in food and beverage products as part of the fermented trend. But there's a little bit, particularly on North America, of pre-fatigue in dietary supplement confusion in the category.

So I would not reach the conclusion that we are losing share just that there's been – the category in the U.S. has slowed down, for sure, in dietary supplements, as well as in China in dairy. But infant formula and many other categories continue to see high growth.

As far as Food Cultures & Enzymes and pricing, one of the key things that I love about Christian Hansen is the discipline on pricing execution. And I don't think there is a lot of – that there will be a lot of more volume to be gained by reducing pricing. I think our pricing really commands to the value that we bring to customers, and you can expect us to continue to be very firm on pricing and gaining volume through the customer proximity and execution of our projects.

Soren Westh Lonning: Yes. And in terms of the early announcement, refer back to that question, Heidi, I mean, this is really driven not by sending messages. It's simply a reflection of us reviewing the sales outlook with the latest information that we have, discussing that urgently with the Board and then coming to the conclusion that we needed to lower the sales outlook for the year.

To an attitude where we believe that – that would suggest, you can say, the rationale investments to really trade on it. So according to the rules based on that, we really didn't have any choice but to go out shortly after we came to that conclusion. So that's really the reason for us doing it, so you should not read any further messages into it.

Heidi Vesterinen: And then in terms of the pricing, so given that anecdotally we hear that other players in the market are pricing more competitively, is this not going to be an issue in terms of volumes going forward? Will you not have to sometimes forgive pricing to maintain customers?

Mauricio Graber: Are you talking about overall or dietary supplements specifically or what category?

Heidi Vesterinen: Probiotics, supplements, dairy, Cultures & Enzymes where you have other competitors which are apparently priced at much lower price points. Is that not going to be an issue when you have a slowing market or challenges in the market? Is there not a risk that we see price erosion overall more towards your competitors' level?

Soren Westh Lonning: So Heidi, I hear you on for sure when there's lower growth that tends to be more pricing pressure on competitive dynamics. But we have had that all along to be honest. It's not new. We compete in all our businesses with formula with competitors in Natural Colors, in Food Cultures & Enzymes and as well in Health & Nutrition.

But the Christian Hansen value proposition has always been about good science, solid solutions and value to customers. And I think we will continue to price on having a value proposition that the customers accept. So I don't see us moving into a more of a pricing-driven category when we are a highly specialized company, bringing new technology and differentiated technologies to customers.

Heidi Vesterinen: Thank you.

Operator: And your next question comes from the line of Ben Gorman. Your line is open. (Your line is open, please go ahead.)

Ben Gorman: Hello, can you hear me?

Male: Yes, go ahead.

Ben Gorman: All right, sorry. (I dropped off the line earlier) so apologies if I'm repeating a previous question. Just two quick ones. First one, in terms of Animal Health, how big of an issue is a maybe more structural market share loss of U.S. beef to Canada and Japan in export markets? Is that part of what's the driving the weak volumes against arguably, the easiest comps so far of the year in beef? That's the first one.

And then secondly, one, just in terms of the comps that you're coming up against in Q4 and Q1 in Plant Health, can you remind us of the contribution to growth from Plant Health in those quarters last year? And then just maybe just in relation to that, whether you think investments in Q4 related to Plant Health launch in North America are likely to be greater on the operating cost side than you've already seen throughout this year so far? Thanks.

Soren Westh Lonning: Let me address your question, Ben, at least the first one. On Animal Health and specifically on beef, when these trade lines are influenced, it has some effects but I would say that the core measures on beef is really that that is a category that we have been able to lift the momentum through dedicated customer wins, and basically, helping increase the penetration in the category.

So beef actually performed well in Q3 for Christian Hansen. The two pain points that we really had in cattle was related to dairy cattle, where the economic situations still remains challenging, although slightly improving. And then secondly, also silage, which is also used for dairy cattle. And this is – the silage category is a category that is impacted also by weather conditions.

So when there is a flood or heavy rains in some areas and drought in other, that influences the amount of silage that is being (bought) and applied to the harvested feed for the animals for wintertime. So in cattle, it's really more dairy, and the silage part has been a disappointment over the beef where we actually saw really good progress in this one. And I may also add in that connection, we saw the same picture in (culture) where we also had good wins that help lift the business.

On the other one, on Plant Health, I would try to avoid going into too much detail on Plant Health given the size of the business. What I would say is that we had a very strong Plant Health in Q4 last year and that the timing this year looks to be a little bit more balanced between the quarters.

So the strong impact from Plant Health will be – we expect that to be less in Q4, simply from timing of when we are supplying our partner in this area here. And in terms of the – but that doesn't really change that we have a very good momentum in Plant Health and it's looking very promising when we look ahead.

When it comes to the operating leverage, et cetera, I mean, it's not something where we see a huge impact from that. It may have a slight negative impact in Q1, but it's not a major concern to us. Bear in mind also that the U.S. is – we have basically now getting the registration in the States and the window for selling into next year in the U.S. is very short, and we don't expect a material impact for this planting season from the U.S. this time around.

Ben Gorman: And actually, on the cost side as well? So I get your point in terms of little impact next year in organic in the U.S. but do you all need to spend a fair amount in terms of operating cost on top of (inaudible)?

Mauricio Graber: Most of the cost that we have in Plant Health is linked to innovation. So, developing new product that can be launched in new markets, and registration and trials for doing that. The actual launch is very much the responsibly of our FC&E partner to buy that out in the market, once the product has been developed and registered and trialed – (trials) there to being supported. So that will be more with our partner.

Obviously, when something is being launched, we will also add some commercial tech people, too, as resources. So, of course, there will be some cost, but the majority of that will be really carried by our partner in FC&E.

Ben Gorman: OK, thanks. Thanks very much.

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

James Targett: Hello, good morning, James Targett from Berenberg. Just coming back on China, a couple of questions. Could you can just contextualize a little bit in terms of the negative growth in Q3 what your growth in China in Food Cultures & Enzymes was in '18 and H1 '19 so just I can (inaudible) get clear on the progression?

And then, you mentioned that it's going take a while to just to reposition your (inaudible) customers or to get the innovations through. But are you expecting negative growth to continue over the next few quarters?

And then regarding the slowdown in growth, could you just talk about how much was down to the underlying fermented milk market slowing versus your – some larger – what some of your large customers changing their amount of business they do with you or stopping to use some of your products? Thanks.

Mauricio Graber: Yes, I would say, I would not give you detailed information on how we do in China on a quarterly basis. But what I would say is that we did see a change in the momentum in our China business towards the end of Q3, start of Q4 last year, also driven by the fact that the market growth was coming down from double-digit and into high-single digits.

So you can say the baseline as we move into Q4 and especially next year will become easier from that point of view. When – when it comes to whether or not we foresee negative growth in the coming quarters, I mean it's definitely not what we plan for. We target to bring it back into growth.

That means that I will also just – there's always a risk when you come from a negative territory to how fast can you accelerate into the state where we need to be. So it's definitely not our plan, but this is also the reason why we give a little bit of caution – it sometimes takes a bit of time to turn the dynamics around.

And I think your third question is related a little bit to where the market is at the moment, and what we are seeing is this mid-single-digit growth in the market and coming from a double-digit growth 18 months ago or so.

So we have seen it coming down and we have seen some movements in terms of volume price components and which categories are going that have influenced us beyond the slowdown in the market in this quarter here. So that is what we are working on to turn those around with customers and bring new value-added concept that can help us also expand growth beyond the market.

James Targett: OK, thank you.

Operator: No further questions at this time. Please continue.

Mauricio Graber: So with that, we would like to thank everybody for joining the call. I hope we were able to provide you better comments and insights into our Q3 performance, our revised growth guidance for the year and our conviction to our long-term financial aspirations. Thank you very much.

Operator: Thank you, and that does conclude our call for today. Thank you all for participating. You may all now disconnect.

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