

**CHR. HANSEN HOLDING A/S  
Q1 2019/2020 Results  
Conference Call Transcript**

15 January, 2020  
9:00 a.m. GMT

Operator: Thank you all for standing by. Welcome to the presentation of Chr. Hansen's Results for Quarter 1 2019 and 2020. 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," "1" on your telephone.

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

Mauricio Graber: Good morning, everybody, and welcome to today's conference call on Chr. Hansen's Q1 2019, '20 Results. First of all, our CFO, Søren Westh Lonning, the IR team and I would like to wish everybody a happy New Year, and we hope you had a good start into 2020.

Before we start, please take notice of the safe-harbor statement on the next slide. Thank you.

Let's continue to Page 3. Chr. Hansen had a mixed start of the year, in line with expectations. Headwinds in emerging markets, normalization of inventory levels in our distribution chain, raw material price declines and order timing negatively impacted our Q1 results, leading to 1 percent organic growth for the first quarter.

Group EBIT margin before special items was 25.7 percent, down 60 basis points, mainly because of lower sales momentum in Health & Nutrition, but also, we continued to invest in growth opportunities and innovation across

our 3 business areas. Free cash flow before acquisitions and special items was minus EUR 6 million, an improvement compared to Q1 last year, driven by a positive cash flow from operations.

On segment level, please turn to Slide 4. Let me start with Food Cultures & Enzymes that delivered a good organic growth of 4 percent, driven by all product areas, except probiotics. This performance needs to be seen in the broader market context, where end-market growth has come down noticeably.

Furthermore, the segment was negatively impacted by the normalization of inventory levels in our distribution chain, where we saw a buildup in the second half of the year because of lower end-market demand. In Health & Nutrition, organic growth was, as expected, negatively impacted by the order timing in human and plant health, leading to a decline of 4 percent for the segment.

Also bear in mind that Health & Nutrition had a tough comparable with 17 percent organic growth last year in Q1. On a positive note, Animal Health reported a very strong quarter. Our business momentum in the U.S. further accelerated on the back of improved cattle farmer economics.

Lastly, Natural Colors reported minus 1 percent organic growth due to continued negative raw material prices impacts and challenging market conditions. Excluding annatto and carmine, where we saw the largest price decreases, the division will have posted slight organic growth as FruitMax range again delivered very strong growth. All in all, not a great quarter, clearly below our ambitions, but in line with expectations and also in line with what we have communicated.

Please turn to Page 5 to talk in more detail about external factors that are currently affecting our performance. When we gave the guidance in October, we took a cautious stance for the current financial year, but it has become clear over the last 3 months that the headwinds are more persistent than what we had initially expected. Doing business in emerging markets remains challenging for different reasons. As a result, our customers see

demand for their products dropping and are increasingly under pressure to save cost instead of bringing new innovations to market.

Well, to a certain extent, in Food Cultures & Enzymes, we can help customers drive efficiencies. For example, with CHY-MAX Supreme, our newly launched chief enzymes, the lower end-market demand does not leave us unaffected. Moreover, some of our larger customers are also losing markets from here to smaller competitors and startups.

In China specifically, the yogurt market has slowed beyond our mid-term estimate of mid-single-digit growth. Most recent market reports indicate that market volume growth is flat or even declining, driven by the steep rise of food prices triggered by the African swine fever and ongoing trade disputes with the U.S.

Within the yogurt category, the shift to ambient away from chilled probiotic yogurt remains a further negative for Chr. Hansen as it limits our upselling opportunities. In Natural Colors, not only the adverse economic climate, which hampers conversion to more expensive natural solutions, caused us a headwind but also continued low raw material prices.

Unlike expected, carmine saw another price decline of 10 percent in Q1, even though the prices were already close to historical lows last quarter. And this, of course, will continue to impact our sales prices throughout the year.

Lastly, we are clearly seeing structural slowdown in the dietary supplement market in the U.S. and Europe. And this, we believe, is because the consumers are confused about which probiotics to take and trying out alternatives to build, such as fermented beverages – fermented foods and beverages. But we are taking action to improve momentum, even in this more challenging market environment. Please move to the next slide, Slide 6.

Last quarter, we talked about the execution. And let me assure you that we have made the necessary organizational adjustments and taken the

measures that were needed to address this. In a market that is more demanding, we are – we have accelerated our efforts to drive sales execution, and we have made good progress on key initiatives that were presented to you last quarter. In Food Cultures & Enzymes, the focus is very much on driving commercialization of recent launches, upselling and developing our adjacencies, and here, we are well on track.

Our recent innovations have been very well received by customers. And here, I would like to highlight, once again, CHY-MAX Supreme that has gotten off to a very good start, particularly in Latin America, but also NOLA Fit, our lactase enzyme. Furthermore, two of our recent launches were recognized as finalists or winners at one of the industry's most important trade first, clearly speaking to the innovation strength of Chr. Hansen.

We are also making good progress on our business with fermented plant basis, where we have engaged in more than 150 customer projects over the last 12 months. We are investing in strengthening our product portfolio and offer our customers a high-performing culture range which tailored solutions to the different plant basis.

In bioprotection, we delivered double-digit organic growth in Q1 after a very soft fourth quarter, and we have accelerated our R&D efforts to bring the third generation to market which will be a catalyst for our growth in Asia Pacific. With regards to China, the slowing yogurt market clearly remains a challenge. Given our success in the past, there are limitations as to how much more we can grow in the established business by increasing our share of wallet.

And let me be clear, I do not expect us to get back to the historical growth rates of high double digits. While we continue to see growth opportunities, particularly in the SME segment and the low-tier yogurt space, what's most crucial for us is to defend our existing business also in light of competition.

Beyond that, I believe the key driver for future growth in China will be innovation. And you hear us talk about probiotics, but also in the probiotic

space, we believe we can innovate and bring new solutions that will help revitalize the market.

Turning to Health & Nutrition. I am pleased to report that we brought to market the new products in Q1, as announced at our last conference call. In Human Health, we launched a new probiotic strain blend for infant, which has shown to reduce the risk of necrotizing and tocolysis, the leading cause for mortality in preterm babies, by up to 50 percent.

Furthermore, our probiotic strain, BB-12, which has been described in more than 300 scientific publications, is now available for organic formulations and can be sold into the super-premium infant segment. Additionally, at our Human Health sales meeting, we introduced some interesting new concepts that we are currently presenting to customers. At the same time, the team is working to further expanding our customer base and geographical reach in emerging markets.

In Animal Health, we recently launched a new dairy probiotic, Bovamine dairy plus, which has seen very good take-up in the U.S., and we continued to roll out GalliPro Fit, our poultry probiotic. Furthermore, we are strengthening our route to market via direct selling where it makes sense and through closer cooperation with our distributor network.

Moving on to Plant Health. The quarter was once again impacted by the order timing from our partner, FMC, but we are on track to deliver on our strategic road map. Today, the team is running more and more projects and crops other than sugarcane, and we're also expanding our geographical reach with the entry into the U.S. market.

Trials with growers are in progress, and we expect first sales contribution this year, though at a very low level. Furthermore, our bionematicides were recognized as the best new biological product at the Agribusiness Intelligence Crop Science Forum, clearly showing that the innovation that Chr. Hansen has delivered in the crop protection space is important and something we can build on further.

Lastly, with regards to the Human Microbiome lighthouse, I am pleased to report that BacThera, our joint venture with Lonza, has appointed Lukas Schüpbach as its new CEO and is having advanced dialogue with different microbiome companies that are highly interested in working with BacThera in the rapid evolving life biotherapeutic space.

For Natural Colors, the strategy is focused on the segments with the most attractive growth prospects, and I am pleased about the progress in our coloring food range, FruitMax, where we continued to gain market share. Furthermore, the team is working on driving conversion in the U.S. and expanding our business into pet food and the food service channel. Raw material prices are expected to remain low for the rest of the year. And instead of competing on price with low-cost players, the division continues to focus on driving profitability.

And with this update on our key initiatives, let me move on to the regional performance on the next slide, please. Group growth in the first quarter was driven by the Americas, whilst EMEA in APAC reported negative growth in light of low-end market demands and customer order timing. Organic growth in our largest region, EMEA, was down 4 percent, driven by declines in Health & Nutrition and Natural Colors. In Health & Nutrition, order timing in Human Health, in dietary supplements more specifically, was responsible for the weak performance.

While in Natural Colors, we continued to see a negative impact from lower raw material prices, but also from lower volumes in selected pigments. Food Cultures & Enzymes delivered decent growth, despite the continued weakness in the Middle East. The region was also impacted by the normalization of inventories at our distributors. North America delivered 7 percent organic growth with a very strong performance in Health & Nutrition, which was driven by Animal Health and good growth in Natural Colors, stemming above all from the coloring foodstuff business.

Food Cultures & Enzymes was on par with last year. Our chief production volumes were only growing slightly and sales in probiotics and wine declined. Latin America reported 9 percent organic growth with very strong growth in

Food Cultures & Enzymes, despite the inventory normalization as we saw really good uptake of CHY-MAX Supreme, the chief enzymes. Health & Nutrition declined because of the order timing in Plant Health, and Natural Colors delivered solid growth, driven by new customer wins, despite continued raw material price headwinds.

In Asia Pacific, organic growth was minus 2 percent, with a decline in Health & Nutrition, which was mainly due to order timing and very high comparables in Human Health. Food Cultures & Enzymes delivered slight growth for the region, whilst China grew solidly with strong growth in fermented milk, which was offset by the continued decline in probiotics.

As already said, the overall market dynamics, though, are unchanged with continued high food price inflation and end consumer preferring ambient over chilled and probiotic yogurts, a trend that is negatively impacting our mix. Lastly, Natural Colors performance was on par with last year.

With this, I would like to hand over to Søren for the segment reviews and the group financials.

Søren W. Lonning: Thank you, Mauricio, and welcome also from my side. Please move to Slide #8 for the segment review. In Food Cultures & Enzymes, momentum improved slightly in Q1 compared to the last quarter. Organic growth was 4 percent, with a 3 percent contribution from volume and 1 percent from price.

And this, despite a continued decline in probiotics and the already mentioned normalization of inventory levels in our distribution chain, which had a negative impact of around 2 percentage points. There were no material contribution from euro pricing.

I would further like to emphasize that, as Mauricio already alluded to, end-market growth is currently tracking at a very low level, with fermented milk growing only 1 percent to 2 percent and cheese only growing around 1 percent globally, adding up to between 1 percent to 1.5 percent growth.

This is clearly below the base assumptions in our growth model, which assumes around 3 percent fundamental market growth. If we look at the performance by product area, fermented milk, enzymes, meat and wine grew solidly in Q1, whilst cheese delivered good growth, and bioprotection reported approximately 10 percent organic growth, driven by fermented milk and meat.

The decline in probiotics continued to be related to China where probiotic yogurt consumption is currently declining. At the same time, in the U.S. and Europe, large legacy brand owners continued to lose shares to smaller players, which was a net negative for Chr. Hansen.

Looking at profitability, the EBIT margin for Food Cultures & Enzymes increased by 40 basis points to 32.1 percent as we continued to see scalability benefits from our Copenhagen site expansion come through.

In Health & Nutrition, please move to Slide #9. Growth was negatively impacted by timing of orders in our Human and Plant Health businesses whilst Animal Health recorded a very strong quarter, supported by improved cattle farmer economics in the U.S., a positive impact from a late silage season and the rollout of our new probiotic offering for dairy cattle called Bovamine dairy plus.

Organic growth for Health & Nutrition, overall, though, was minus 4 percent as Human and Plant Health, both declined as expected. Whilst in Plant Health, order patterns should be back to normal as per Q2, we take a more cautious stance for Human Health. Our dietary supplements customers continued to face a challenging market with increasing competition from players without scientific documentation and end consumer still struggling to choose the right product.

As a result of this, our customers are delaying projects and taking down expectations. In infant formula, on the other hand, the tailwind that we've seen from new brand registration rules in China over the past 24 months is fading. Whilst overall, the outlook for probiotic to infant formula is still



positive with double-digit market growth, FY '20 will be a challenging year, given the high comparable that we face.

Looking at profitability for the segment. The lower sales momentum had a negative impact on the EBIT margin, which came in at 19.6 percent, 5.8 percentage points lower than last year. Another reason for the decline in profitability was slightly higher R&D spending for Plant Health.

Moving on to Natural Colors on the next slide, Slide 10. The division reported minus 1 percent organic growth as our traditional Natural Colors business continued to be challenged by declining raw material prices for carmine and annatto as well as a generally more challenging economic climate in emerging markets.

On a positive note, our current foods business reported very strong growth, particularly in EMEA, and we delivered solid growth in LatAm due to recent project wins. Looking at profitability, the division was able to increase its EBIT margin, thanks to the lower raw material prices by 1.1 percentage point to 12.0 percent and increased the absolute EBIT by a full 10 percent.

Let's now look at the group financials and the cash flow on the next page, Page 11. Group organic growth was 1 percent, all driven by volume. Currencies had an immaterial impact. If we look at profitability drivers, the gross margin improved by 0.4 percentage points year-on-year, driven by scalability benefits in Food Cultures & Enzymes and lower raw material prices in Natural Colors, partly offset by negative scalability in Health & Nutrition due to the lower sales. As Mauricio already alluded to, we continued to reinvest in future growth and our strategic priorities, resulting in a 1 percentage point increase in operational expenses in Q1.

Higher investments in R&D were mainly related to Food Cultures & Enzymes and Plant Health, whilst the increase in sales and marketing was mostly attributable to Food Cultures & Enzymes and Natural Colors.

Overall, this led to an EBIT margin before special items of 25.7 percent for the year, down 60 basis points. Special items amounted to EUR 1 million,

primarily related to costs associated with our BacThera joint venture, leading to an EBIT margin for the group of 25.4 percent. Please remember that our investments in BacThera is listed under net financial items in the P&L, where we reported a small loss this quarter as expected and as an investment in associates in a separate line in the cash flow statement.

Turning to the right side of the slide. Free cash flow before acquisitions and special items was an outflow of EUR 6 million compared to an outflow of EUR 33 million in Q1 last year. The improvement was driven by the positive cash flow from operating activities, which was due to a favorable change in net working capital and lower taxes paid.

Cash flow used for operational investing activity was 10.6 percent of revenue compared to 11.1 percent last year. For the full year, we expect CapEx to end above the prior year level of EUR 139 million, driven by our expanded investment program. And with this, I would like – I would now like to move on to the guidance slide on Page 12.

Even though Q1 was very much in line with our expectation, we do narrow our organic growth guidance range for 2019, '20, in light of lower end-market growth to now 4 percent to 6 percent compared to 4 percent to 8 percent before, with an expected neutral impact from euro pricing. In the remaining 9 months of the year, Food Cultures & Enzymes and Health & Nutrition, in combination, are expected to grow around 7 percent compared to 7 percent to 10 percent before.

Food Cultures & Enzymes is now expected to grow 5 percent to 6 percent, which is significantly above the current low momentum in the dairy end market. This is around 1 percentage point lower than what we previously assumed. The growth expectation for Human Health have also been lowered because of delays of customer projects in dietary supplements, whilst expectations for Animal and Plant Health remain largely unchanged as both are expected to deliver strong growth.

Lastly, Natural Colors is still expected to grow low to mid-single-digit in the remaining 9 months, driven primarily by continued growth in coloring foods, but partly offset by lower raw material prices. The other two guiding metrics are unchanged. EBIT margin before special items is still expected to be around 29.5 percent.

Increased utilization of production capacity in Food Cultures & Enzymes will have a positive impact on the margin, which will – which is expected to be offset by selected investments into the lighthouse projects and other strategic priorities. Free cash flow before acquisitions and special items is still expected to be around EUR 190 million, with CapEx above the EUR 139 million that we realized last year.

And with this, I would now like to hand back to Mauricio to talk about our long-term ambitions.

Mauricio Graber: Thank you, Søren. Whilst at this point in time, our strategy review process is still ongoing, preliminary results indicate that the headwinds we are facing at the moment are not all of short-term nature, which is why we not only narrowed the guidance range for our current financial year but also had to revisit our long-term growth ambition.

As part of the strategy process that we are conducting a thorough review of the growth opportunities in our different end markets, our R&D pipeline and current customer initiatives. The preliminary conclusion does not support Chr. Hansen maintaining the current long-term growth ambition of 8 percent to 10 percent until '21, '22 with Food Cultures & Enzymes delivering 7 percent to 8 percent.

There are 3 main reasons for this. First, fundamental market growth in Food Cultures & Enzymes is approximately 1 percent lower than the previously anticipated 3 percent, and this is because of the expected lower growth rates in emerging markets as well as the decline in fresh dairy consumption per capita in the U.S. and Europe because of consumer preference shifts.

Second, the structural changes in the dietary supplement market means that we expect Human Health market to grow at a slower pace than previously expected. And third, Natural Colors. For Natural Colors, if we leave the raw material prices impacts aside, conversion is progressing slower than what we had anticipated, and we don't see any key indications that this will change absent of regulatory incentives.

Taking all of these factors into consideration, as a management team, we don't think that 10 – the 8 percent to 10 percent group organic growth until '21, '22 is longer feasible, which is why we decided to issue a new preliminary long-term growth ambition of mid- to high single-digit growth for the group until '24, '25.

The group long-term ambition on EBIT margin and free cash flow until '20, '21, '22 remain unchanged for the time being but, of course, we will review together with the preliminary growth ambition as we are completing our work on the strategy. A new set of long-term financial ambitions for the period until 2024, '25 will be finally confirmed and announced at the Capital Markets Day in April.

To wrap up, please turn to the next page. Q1 2019,'20 was in line with expectations, but current end-market challenges are proving to be more persistent than we had anticipated 3 months ago. As CEO, I clearly dislike delivering negative news in the form of a downward correction to our growth outlooks, but as management, we are committed to providing our shareholders with full transparency and our best assessment of the current situation.

Overall markets have turned less positive, but that doesn't mean that we are standing still. We have made good progress on our key initiatives, strengthened sales execution across the organization, further advanced our commercialization pipeline and seen really good early update of our recently launched product.

I continue to believe very strongly in Chr. Hansen's mid- to long-term growth opportunities and our unique technology platform. And whilst we have lowered our long-term growth ambition, Chr. Hansen still has the ambition to continue to significantly outperform its end markets. I am convinced the current challenges will strengthen our organization and make us more resourceful in winning with our customers.

There remains many attractive growth opportunities in the microbial and natural solution space. It is amazing all the things that we can do with the power of good bacteria in solving some of the society's largest challenges. And I am looking forward to sharing the results once we have completed our strategy process in April at the Capital Markets Day, for which you can now sign up in our IR website. Chr. Hansen is an ambitious company, and we are doing everything we can to accelerate momentum and create value for shareholders in the current market conditions.

With this, I would like to open up the call for Q&A. Thank you very much.

Operator: Thank you. For the questions and answer session, participants are kindly asked to limit themselves to three questions only. As a reminder, if you wish to ask a question, please press "star," "1" on your telephone and wait for your name to be announced. If you wish to cancel your request, you may press the "hash" key. Once again, "star," "1" if you have any questions. The first question is from the line of Lars Topholm from Carnegie.

Lars Topholm: A couple of questions on my side. So on the new long-term growth targets, do you expect this mid- to high single-digit range to be narrowed in at the Capital Markets Day on the 22nd of April? And specifically for Food Cultures & Enzymes where you have lowered the underlying market growth by 100 bps, do you see any change in the potential additional growth you can deliver on top of the underlying market growth or sort of that discrepancy the same as before?

And second question is, you mentioned that you have accelerated 3G bioprotectants. Can you comment a little bit more on what that means relating to timing of when this is launched? And what it means in terms of

reaching growth? I still think you need to grow close to 30 percent CAGR to reach your lighthouse ambition for bioprotections. Is that realistic? And then a third question, which is more technical.

So with BacThera, your human biome investments and end expenses are clearly going into a company which is booked as financial expenses, does this mean that you are to factor moving expenses out of Health & Nutrition, which will now be reported below the EBIT line?

Mauricio Graber: Thank you, Lars. I will take a couple of the questions and then pass it on to Søren for completion. So on your question about guidance, the whole purpose of issuing the interim guidance was to be transparent and, obviously, we cannot comment more on this until we have the time to complete our full strategy assessment and come back in April with what we believe is the guide – the right long-term ambition for our business based on the 5-year strategic priorities.

So I appreciate timing on that. And in Food Cultures & Enzymes, as we have indicated in the text, our ambition is to continue to significantly outgrow the underlying market with our innovation, expansion, market share, customer engagement so you can expect that model of Food Cultures & Enzymes to continue to play on a multiple outperformance of the market.

Lars Topholm: That I understand, Mauricio, sorry, if I can just comment on that. So does that mean for Food Cultures & Enzymes isolated scene, the moving part is really the underlying market growth and not anything else?

Mauricio Graber: That is the major moving part of the change in Food Cultures & Enzymes. I think what you also have to look and take into consideration, Lars, as we look 5 years ahead, is we'll continue to have a larger conversion level in our DBS, but the most material change for sure is the underlying market.

To your second question on the third-generation bio-p, I wouldn't say anything different for what we say in the last call. We think that would be 18 to 24 months away that we can really introduce that to customers. But there's a lot of priority being placed on that. And obviously, any incremental

improvements that we find between the second and a full-blown third generation, we will sequentially bring that into the market.

I would say I have a high level of confidence on the relevance and the potential of bioprotection for Chr. Hansen. But we will come back in April in the Capital Markets Day because – revisit when the EUR 200 million can be achieved. I think you are right that a 30 percent CAGR is probably not realistic. Søren, I will pass it on to you for the BacThera question.

Søren W. Lonning: Yes. And regarding BacThera, you can say that there has been a small transfer of both costs and also a little bit of business, you can say, from Chr. Hansen to BacThera as part of this change, but it's quite small numbers overall. And the net impact on EBIT is immaterial in the larger scheme of Chr. Hansen.

The key, you can say, impact in BacThera relates to new hirings in the company, new establishment in the company and investments made after we have closed and created the – closed the transaction and created the joint venture formally.

Mauricio Graber: I think I would just add to that, Lars, that the investments that we're doing in BacThera really to have the large capabilities to be able to supply under farmer conditions to the customers according to the CDMO model of BacThera.

Lars Topholm: Yes, I understand. I was just asking because theoretically, one could argue for higher margins in Health & Nutrition, if expenses are transferred to below a bit, but it wasn't that lucky.

Operator: Our next question is from the line of Søren Samsøe from SEB.

Søren Samsøe: Søren here. Just in regards to your – both your this year's guidance and the coming year's guidance, I mean I don't think I've heard you use the market growth as a primary explanation for your own growth. So I was just wondering why – something has changed that makes sure you're more

dependent on market growth than we have seen in the past and what that could be?

And then secondly, regarding the inventory adjustments of 2 percent in Food Cultures & Enzymes, first of all, if you could just elaborate a little bit what regions and what clients are we talking about here? What's the reason for the inventory adjustments? And where are they? And also secondly, if you can quantify if there would be an inventory effect in Q2 and Q3 as well?

Mauricio Graber: So on the overall guidance, I think, Søren, you are right, which is we operate as an innovation company that outgrows the underlying markets by a multiple. But when there are significant changes to several of the underlying markets, I don't think we are immune to that. So what we're trying to flag to you in a clear and transparent way today are basically 3 things.

The underlying market growth in dairy has probably moved down by 1 percentage point, from 3 percent to 2 percent. And while we still expect to significantly outperform that, it's definitely more challenging. And that's why we sort of narrow our range as well from 4 percent to 6 percent. But you can see from our guidance on Q2 to Q4 that we still expect the microbial platform to have a strong performance, and with that, Food Cultures & Enzymes as well as a multiple of that underlying market.

The second one is Health & Nutrition, really dietary supplements is a big challenge. And while we are committed as a leading company to the future of probiotics in microbial solutions and got held in the whole opportunity that this represents, we will need to find a way to innovate more in this segment and to make consumers readjust the growth in the dietary supplements category, specifically.

And the third one is Natural Colors, where you see that the conversions of large brands are slow and far apart. We do see on the positive side, new product introductions, mostly being launched with Natural Colors. I hope this provides you some colors – some color to the question. Søren, I will pass it to you for the...



Søren Samsøe: Sure. If I could just follow-up. I mean, OK, so that's fair. But then I don't hear you say that anything has changed in your, you can say, in the competitive advantage, in the pricing situation or in the competitive situation, that nothing has changed there. That's not what I hear you say.

Mauricio Graber: That's correct. I think we feel quite strongly on our – if you look at the fundamentals of our business, Søren, of saying, it's a business with high barriers to entry, high switching costs for customers, and where we hold a lot of innovation and strong pricing power.

I think that is reflected in the strength of our EBIT performance and in our performance overall. We are going through a moment of a more challenging growth period. That, I have the confidence, as a team will be able to address, but we need to confirm the fact that the growth has been more challenging.

Søren W. Lonning: Søren, regarding your question on the inventory adjustments. If you look at the regional drivers, this has been primarily been in the emerging markets and with Middle East and Asia outside China as the key areas. And we are seeing that relating to a gradually slowing demand seen during the second half of FY '19 that translated into this higher inventory position.

As we have written in the announcement, we believe we are roughly 75 percent completed in Food Cultures & Enzymes. So we have taken, by far, the majority of the hit in Q1. There will still be a small impact that we expect to – that will hit us in – over the coming quarter, but it will be of a smaller nature than what you have seen here in Q1 for sure.

So we are around 75 percent done. And that means that it's up to 1 percentage point that we still have to go in a mission in a single quarter that we have, but the majority is done.

Operator: Our next question is from the line of Jonas Guldborg from Danske Bank.

Jonas Guldborg: First, if I can go back to dietary supplements, could you just repeat and also elaborate on what it is that is fundamentally changing your outlook longer

term? And also, in that perspective, is there anything you can do – elaborate on what you just said you could do to kind of get you out of this lower-growth prospects? Then secondly, this was your fifth quarter with the organic growth below 20 percent in bioprotection.

Is it rightly to assume that the challenges you experienced from the beginning of last year is now annualized and then from Q2, we should see a higher organic growth – significantly higher organic growth for bioprotection? And then my last question is on Natural Colors. Now you're lowering your longer-term outlook for Natural Colors growth.

So it's clearly not supporting your overall group organic growth expectations. Does that change your view on your ownership of this business?

Mauricio Graber: Thank you, Jonas. I think on dietary supplements, I would say, we have seen a weak dietary supplement market across key markets, mainly, I would highlight the U.S. where there has been really what we call bill fatigue and a lot of offering of undocumented strains, creating a lot of confusion with the end consumer.

And I think the whole category and the shift that we have seen also to online has made the whole dietary supplement category in the U.S. go down to very low levels of growth. We have also seen in Europe, some of the largest dietary supplement markets like Italy soften. And even in China, the dietary supplement markets have also been slower.

So I think you're seeing a bit of a more systemic slowdown in the category. And by the way, I want to differentiate that from infant formula, where we continued to see a higher penetration of probiotics in infant formula, and we're excited about the growth opportunities that, that represents. What we have to do in the dietary supplements category as a leader in that category is to innovate together with our customers, to continue to drive science of the consumer, make the right choices.

And I think in the call today, I gave you some really good examples on how we are leading with BB-12 and LGG to bring specific products that resonate with the key consumer needs, and we will continue to invest in building our strength in the dietary supplements category.

Bioprotection, I think we delivered 10 percent growth in Q1. I – what I stated is that bioprotection represents a large opportunity across the fermented categories. And also in the future to expand to some other categories as we have mentioned. But the technical challenges are higher to overcome. And therefore, I think we need to come back to how fast will bioprotection grow.

Probably, if you have to take a best estimate, I would take Q1 as the best estimate of saying we expect bioprotection to continue to deliver double-digit growth, but I won't project that to the higher end of 20 percent. NCD, Søren, do you want to comment?

Søren W. Lonning: Yes, I think the – we're in the middle of a strategy process. And as part of that, we are obviously always reviewing the – both the growth outlooks within our businesses, but we are also considering the entirety of the portfolio. But we have no work ongoing to change at this point, but it's a natural thing that is embedded in this strategy process, and that's the only thing really to say about that at this point in time.

Operator: Our next question is from Heidi Vesterinen from Exane.

Heidi Vesterinen: So the first question, I think in your speech, you said that you're needing to defend your position in light of competition in China. Could you elaborate on what you meant? That's my first question.

Mauricio Graber: We see a more competitive market in China. I think, as I've mentioned several times, Heidi, we have a very high market share in China, higher than our average Food Cultures & Enzymes market share. And therefore, you can expect that when a market slows down, like it happened in China, there's more competitive pressure.

And therefore, we need to make sure we do 2 things in China. One is that we protect and develop our established base with the large Chinese customers. And second that we continue to build the SME market and the innovation in the areas where we're not playing. And that sort of summarizes our game plan in China.

Heidi Vesterinen: So when you say competitive pressure, is it new entrants or is it existing entrants being a little bit more aggressive? So does that mean there was price pressure in the market? Just to clarify.

Mauricio Graber: I don't think we have seen any large new entrants into the Chinese market. So it's the established customers are fighting for market share in large customers that have all of a sudden seen a deceleration of growth. And as I mentioned in my speech as well, there is more focus on cost management as they're trying to manage to these more subdued market.

I do believe our interactions with the Chinese customers is they all know they have to innovate their way in to continue to expand the dairy market share in the Chinese market.

Heidi Vesterinen: And then the second question. I think you had said in your speech that in the U.S., large legacy customers are losing share to smaller companies. And I think this was an FC&E comment. I thought I had understood that you have quite a fragmented customer base in that no individual multinational company matters. Had I understood that incorrectly? Or is there a new development? Just to clarify.

Mauricio Graber: The comment was global, Heidi, it was not only related to the U.S. And you are right, we have a very high granularity across FC&E, serving very small customers. But when you look at some of the larger brands that had a probiotics in their offering, I think when the volumes there declined, we definitely see an impact in our total probiotics business.

Heidi Vesterinen: And then the last question. Do you have any initial comments on the IFF Dupont situation? As I'm just wondering if these integrated solutions that they're talking about works then – because the concept does seem to make

sense, right? It's just making life easier for customers. Isn't it a risk for you as a focused player?

Mauricio Graber: I think we have seen DuPont be a strong competitor that we respect a lot. We have no major comments really on the sort of IFF acquisition. It will be a long closing period for over a year. Probably a lot of distraction in such a large merger. I think as Chr. Hansen, we need to focus and double down our – in our products and our customers and compete to win in the marketplace.

Operator: The next question, it's from James Targett.

James Targett: Two questions. Firstly, on – coming back on dietary supplements. So am I understanding that the reason for the lower – maybe the lower growth expectations going forward is really coming from outside North America, so a further declining market in – now in Europe and Asia?

Because I think as you – in your report, you called out strong growth in Human Health in North America in Q1. I don't know whether that's more formula driven, but that implies dietary supplements were stronger in North America. So the incremental decline is coming from other countries. So I wonder if you could clarify that.

And if it's just about softer market or whether you're talking about you're losing share within the market as well. And then secondly, on China, I just wanted to sort of, I guess, clarify the momentum in Q1 really. You did – I mean, you mentioned solid growth in China in Food Culture & Enzymes in Q1. I think you were declining, though, in the second half of last year.

And you didn't – and you said there's been no sort of change in the market backdrop. So just wondered if you could talk about Q1 in the context of the second half of last year in China.

Mauricio Graber: So on the dietary supplements, James, I can say that for sure, North America is not where we see the change as the largest one. That's why we have seen a continued challenging situation. We are seeing Europe becoming more challenging, first and foremost.

And then secondly, also, the growth rates in Asia, Asia Pacific has also – even though they are still attractive, they have come down. So those are the 2 key drivers behind the change that we are articulating now. And when you refer to the specifics of the Q1, yes, we did have good growth in dietary supplements in North America in here, but have to bear in mind not to judge the performance of Human Health or Health & Nutrition, in particular, on a given quarter, given that it's rather large customers where all the time, it means a lot.

And overall, it was negative for the quarter, but we – in North America actually had a bit of a tailwind within dietary supplements in terms of all the timing. So don't over-interpretate that. North America remains challenging. And Asia and Europe are the ones that are more – are moving into more challenging territory. That being said, we are coming from a quite high level, and we still project global growth going forward in dietary supplements containing probiotics.

So it's still a very attractive market to pay the two, but it's just at a different level than what we have seen in the past. Then on China, for sure, we had good growth in Q1. I think we benefited from some one-offs on customer allocations and volumes based on our quality and our service. But my expectations for the full year are definitely not as high as we performed in Q1. Anything you would complement to that, Søren?

Søren W. Lonning: No. And you can say the dynamics of probiotics being extra challenging in China is also remaining. So the growth that we delivered in Q1, in addition to, you can say, what Mauricio also build on also reflects that probiotics remains challenging, whereas we were more successful in the traditional fermented milk care cultures in this quarter.

Operator: Our next question, it's from the line of Anton Brink.

Anton Brink: From my side, firstly, could you quantify the destocking effect in Human Health as you do for Food Cultures & Enzymes and as well as the timing

effect in Plant Health? And then secondly, what's the risk of Animal Health ultimately ending up in a similar situation as Human Health appears to be in now?

Mauricio Graber: I think we will not provide specifics as to the effects, but what I can say is that when it comes to Human Health, as an example, we did deliver high single-digit growth last year. And we are also expecting beyond this quarter, which was very challenging that we will deliver a solid growth component in the remaining part of the year in Human Health.

So timing of orders with customers and their launch plans and their order pattern has a huge effect in Q1. And similar for Plant Health, we delivered strong – very strong double-digit growth in FY '19. We also expect a strong growth, double-digit growth, in '20 for Plant Health. So again, the timing effect that we are considering is quite significant in Q1.

In terms of the Animal health business, I would say that here, we are seeing some – generally a better cyclical situation in some key markets, most importantly, North America and the capital situations where the economies of – especially dairy cattle farmers has improved.

So that is, you can say, building some strength into it. We have also seen the silent season, which was poor in – towards the end of FY '19, actually was coming back with a strong season, late season, in Q1. And then we have launched some new interesting products, which have seen a really good uptake in – among our customers, primarily the dairy – volume in dairy plus product that we have out there.

So all in all, I would say that here – on this part here, we are relatively positive in the outlook for Animal Health for the coming year, both in terms of the market and our ability to also capitalize on the great products that we have – we are launching.

Søren W. Lonning: Probably just to add to Animal Health is in addition to Bovamine plus that has had a very good takeoff with some of our – some of the larger cattle

farming segments, we also continued to see a very good performance of GalliPro Fit, our probiotic for the poultry segment where large accounts represent sort of a large opportunity for us to continue to build volume.

So we don't see that. I would just say on Human and Plant, remember that there will be more variations quarter-to-quarter, and the best thing is to look at those businesses on the annual growth performance.

Mauricio Graber: And maybe just one word of pause in terms of the Animal Health. Q1 was very high. So very high double-digit growth in that part of the big business. And that was partly helped by the patent in the silage season. So you cannot just extrapolate that development in the coming quarters, although we expect a strong year in Animal Health this year.

Operator: Our next question is from Faham Baig from Credit Suisse.

Faham Baig: I also have 3 questions. Firstly, just more of a thematic/midterm question. In a number of categories, one of the themes I've picked up is that large customers are losing share to smaller customers/startups. We see that in FC&E, we see that in dietary supplements, we've seen that in dietary supplements for some time.

But it seems like we're beginning to see that in Europe as well. And we're seeing that a bit in China as well. What I recognize from that is that Chr. Hansen, does it have the same relationships with smaller customers as it does with larger customers?

And if I look out to the next, let's say, 1 to 2 years, are you looking to build relationships with the smaller customers to where the growth is? And if so, how long do you think that evolution might take? Is there any impact on the P&L relationships with the smaller customers versus the larger customers? That's sort of my first question.

The second question is with regards to the midterm ambitions, mid-single-digit to high single-digit growth. Appreciating that the market growth has



slowed by 100 basis points, which I guess, at the group level, if we take into account the dietary supplements and Natural Colors comments, it's probably also around 100 basis points, given the size of the businesses relative to the FC&E.

So I'm just trying to understand what deviates the bottom end of the range from 8 percent to mid-single digit, call it, 4 percent, when the market growth rate only has 100 basis points impact? That's my second question. My third question, for FY '20, now if I take into account some of the one-offs in Q1, and your underlying market growth is – so say you're growing 3 percent after taking into account the one-offs.

What could potentially accelerate you to the midpoint of your full year guidance of 4 percent to 6 percent when you're suggesting that China, you cannot extrapolate growth there? In Animal Health, you don't extrapolate growth there, bioprotection is already at double digits. Could you just help us with some of the building blocks because as you suggest, the market growth won't be improving in the second half of the year?

Mauricio Graber: Maybe we'll start with your last question, and Søren and I double tack on that. So basically, if you look at the one-offs in Q1 that we had communicated, the two largest ones were really in relation to the destocking and to the order phasing of Human and Plant. So if you do the math of those, then you clearly get well into the range. But Søren, you may complement that.

Søren W. Lonning: Yes. I think building from Q1 is tricky because we've had quite a few temporary headwinds with order timing and destocking. So I would say there will be some relief here. Also, there will be a baseline in the coming quarters that will be more favorable in some business areas like Natural Colors and also Animal Health.

And then I would say, otherwise, it comes down a lot also to our ability to execute on our customer – our project pipeline with customers. That is really cool because if we are to outgrow the market in Food Cultures & Enzymes by

2 to 3x, it requires that – strong execution of that. That is no different from any other year that we've had.

So you can say there are some baseline things, there are some timing things and then really executing on the pipeline, that is key. When it comes to – maybe to your second question, in terms of the mid- to high single and about how that translates to the – first and foremost, I mean, with mid- to high single digit when we look beyond the year that we're in, where we have a guidance from 4 percent to 6 percent, the mid- to high single digit is a 5 percent to 9 percent that we are thinking of.

And it's true that it's 1 percentage point lower in Food Cultures & Enzymes than previously expected in the market. However, when we look to some of the other segments like dietary supplements, it is a larger impact than the 1 percent. So across all the business areas, actually the impact from market we see as larger than just the one that we – I explained about in Food Cultures & Enzymes. So I think that's the other point to add to that.

Mauricio Graber: And I think we also see, overall, a more volatile environment, right? So there's a lot of trade tensions right now in the world. We talk about the developing markets that have been high growth markets for us. So I think as we issue interim guidance, it's logical that, that interim guidance provides a wide range of mid- to high single digits.

Talking about the customers and large customers shift to more, let's say, local customers, start-ups, more entrepreneurial customers, I think your conclusion on Food Cultures & Enzymes is not correct. We actually have a very large share of serving small customers. We service, we have said in the past, over 4,000 dairies across the world, and we have very deep technical and commercial relationship with smaller customers.

I think, though, as I said, when there's a large decline in one of the large customers, you need to capture volume and growth with many small customers. The situation is different in Human Health, where our business has historically been very concentrated with large customers and where we

need to expand our geographic reach and our customer reach with more probiotic solutions to have a broader market coverage across online and retail to balance our growth profile from a customer point of view.

Operator: Our next question, it's from the line of Arthur Reeves.

Arthur Reeves: Just one question from me, and it's about the medium-term growth outlook. You talk about the market slowing from 3 percent to 2 percent, but what actually is going to make the market improve from where it is now?

You're talking there about 1 percent to 1.5 percent at present, and all the indications that I see for future global milk supply, not demand, but milk supply, are pretty much flat. So what is the thinking behind your 2 percent market growth forecast in your midterm guidance, please?

Mauricio Graber: Of course, this is a careful assessment and a preliminary assessment based on the – where we are now in the strategy process. But we believe that the momentum that we are seeing in the market now both reflects something that is cyclical but also something which is temporary or cyclical. So as an example, the cheese production of around 1 percent right now, which is at 0 in Europe and around 1 percent in North America.

Cheese production is something that moves with a certain cyclicity. And here, the intel that we have from market data, market reports, customer discussions about expansion plans, et cetera, means that we believe that, that number will normalize to a higher level than what we see right now. Similarly, when it comes to fresh dairy, the absolutely largest changes in emerging markets that we see right now with China actually being flat to slightly declining.

And also some other emerging markets like the Middle East suffering right now. And we also believe that although these markets are coming down relative to what we said at the Capital Markets Day 2 years ago, it's – right now, we're also at a special point in time due to some external reasons, and

we believe that we will see some recovery in these markets when we look in a 5-year horizon.

So that's the logic that is behind this number here. But of course, we continue to monitor the development in there very carefully. And that is exactly also why – how to – how our plan for addressing plant-based protein is one of the key topics that we have in our strategy plan because that is also important for us to tap into this market and this trend when we look forward.

Arthur Reeves: And then if I could just have one follow-up, given I didn't start with three, how big a plant based – how – what percentage of your sales is currently plant-based, please?

Mauricio Graber: It's a relatively small proportion of our sales. Bear in mind that based on our knowledge, it's still within yogurt. Plant-based is still at around 1 percent of global yogurt that is plant-based. And cheese is less but reducing acceleration, and we will – we also expect as that market develops further that they will be looking for even better solutions from what they have today. And this is where our cultures can really play a role.

So it is not large for us today, but we believe that it will be a vehicle going forward when we look out to a '25 and, especially, a '30 horizon.

Søren W. Lonning: And specifically, even though, overall, it's 1 percent or less than 1 percent of dairy, obviously, if you look at some specific markets or population segments, affluent metropolitan cities with millennial consumers, the market share is higher.

And that's where we are really working with customers to understand how to deliver the best products to those consumers. And as I mentioned during the call, we are engaged in hundreds of projects on a very successful way with the leading customers in plant-based.

Operator: Our next question is from the line of (Patrick Rafael).

(Patrick Rafael): The first one would be on your lighthouse projects in light of the new mid- to long-term guidance. You've already talked about bioprotection, but can you also talk about your other lighthouse projects and how they're impacted by reduced midterm growth outlook.

The second question would be on cash flow and some particular free cash flow, where you improved year-on-year quite significantly, thanks to lower working capital. Was that already built into your original around EUR 190 million guidance for the year? Or was this a positive surprise versus your budgeting for the quarter?

And then the last question is just on Natural Colors. You mentioned, given the, let's say, subdued growth outlook here, focus will be on margins and improving profitability. Can you provide a bit more color on what exactly you're planning to do here in Natural Colors?

Mauricio Graber: Thank you, Patrick. I'll take the first one and Søren, pass it to you. I would say on the lighthouses, if you remember, we had mentioned 3 lighthouses. I think bio-p, we have commented extensively during the call today. Our plant sales, we continued to be very excited on the momentum which we see in Plant Health with very high growth.

I think we are tracking towards a successful execution of our Plant Health. And the key steps in our Plant Health journey will be to continue to gain acreage in Brazil sugarcane, expanding to soy and then expanding to geography in the U.S. We will also consider other potential expansions that we give our products the best growth, but we are confident on our Plant Health lighthouse.

And we have not quantified the human microbiome lighthouse. But I think BacThera provides us the first entry into the exciting life biotherapeutics market, and we're quite confident that, that will play out as a future success for Chr. Hansen and Lonza on having BacThera be the leading supplier of life biotherapeutics CDMO solutions. Søren, do you want to take on for cash flow?

Søren W. Lonning: Yes. As the cash flow is also – is always a volatile metric in a given quarter. And – but I can say, overall, it was quite in line with what we expected. And that's also why we have maintained the free cash flow for the year. So no big surprises here. And one of the reasons why we came out strong related to a strong cash collection in this month from our customers, that was also a focus area.

So it was built into our plans. When it comes to your question regarding Natural Colors margins, I would say that the – you can say the – I would put it in 3 pillars in terms of the margin management. First one, of course, being managing the raw material fluctuations in a very diligent way up or down, whether that's the case, then we will monitor that carefully and manage the pricing in the right way.

Secondly, I would say, efficiency, especially in our production is a key focus area, and we are continuing to invest in and how we can work more efficiently. And finally, when it comes to what you can call, sourcing and breeding of the raw material components, which is a large part of the cost base in Natural Colors, that is also really an area where we continue to work to improve our margin position and cost and use offering with customers.

So across those three, I would say that those are our key priorities in terms of managing Natural Colors margin in a positive development.

Mauricio Graber: And I think we ...

Operator: And there are no ...

Mauricio Graber: With that, we would like then to thank everybody for their participation in the call and the good questions. Please do not hesitate to reach out to IR in case there are any further questions. Thank you.

Operator: Thank you. That concludes our call for today. You may all disconnect. Thank you all for participating.



*Improving food & health*

END