Chr. Hansen Holding A/S
Q2 2019/20 Results
Conference Call Transcript

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Operator: Thank you for standing by, and welcome to the presentation of Chr. Hansen's Result for Q2 2019/'20. I must advise you that this conference is being recorded. I would now like to hand the conference over to your speaker today, Chr. Hansen's CEO, Mauricio Graber. Please go ahead.

Mauricio Graber: Good morning, everybody, and welcome to today's conference call on Chr. Hansen's Q2 2019/'20 results.

The global COVID-19 pandemic is posting great challenges onto everyone these days. And let me start by saying also, on behalf of our CFO, Søren Westh Lonning, and our IR team that we hope you and your families are healthy and safe during this uncertain and unprecedented times.

As part of the food supply chain and with our ingredients reaching more than 1 billion people everyday, we carry a special responsibility during this pandemic crisis. And let me assure you that at Chr. Hansen, we are doing the utmost to keep delivering to our customers all around the world while safeguarding the health and safety of our employees.

We will, of course, address the business implications of COVID-19 pandemic for Chr. Hansen during this call. But let us start with providing you an update on our performance during the second quarter of our financial year '19/'20, which ended in February, therefore, before the pandemic impacted business globally.

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

Let's turn to Page 3, please. In line with expectations, sales momentum picked up in the second quarter, leading to 5 percent organic growth for the group in Q2 and 3 percent year-to-date. The overall deep business environment though did not materially improve.

Trading conditions in emerging markets, particularly in the Middle East and China, remain challenging. Dairy end markets continue to grow at the low level, and raw materials for Natural Colors remain at very low price points. In light of this, I am quite pleased with the sales performance for the quarter.

Looking at profitability. Group EBIT margin before special items was 28.2 percent in Q2, up 40 basis points as we continue to balance scalability benefits from production and cost management initiatives with investments into strategic priorities and new innovations.

Year-to-date, group EBIT margin before special items stood at 27 percent, which is on par with last year. Free cash flow before acquisitions and special items was EUR 47 million in Q2, up 18 percent, driven by an increase in operating cash flow. Year-to-date, free cash flow before special items was EUR 41 million, well ahead of last year.

On segment level, please turn to Slide 4. All 3 businesses contribute to improved momentum in Q2. Our microbial platform, Food Cultures & Enzymes and Health & Nutrition combined, delivered solid organic growth of 6 percent in Q2, leading to 4 percent year-to-date.

Food Cultures & Enzymes continued to clearly outperform its underlying markets, delivering 5 percent organic growth in the second quarter and 4 percent year-to-date. Health & Nutrition reported 8 percent organic growth in Q2 after a very soft quarter – first quarter, resulting in a year-to-date increase of 2 percent.

The result was driven by a meaningful improvement in Human Health and continued strong growth in Animal Health. And like expected, Plant Health did not perform well as sales uptake in soybean was lower than expected. Lastly, Natural Colors also lifted the underlying sales momentum in Q2, delivering 3 percent volume growth that was largely offset by negative pricing because of lower raw material prices. Year-to-date sales were on par with last year.

Before we go into further details on the financials, as usual, let me also comment on the strategic highlights of the quarter. Please turn to Page #5. During Q2, we have made very good progress across our microbial platform. In Health & Nutrition, new product launches in Human and Animal Health such as our new probiotic strain blend for preterm infants or our new cattle probiotic, BOVAMINE Dairy Plus, were very well received by our customers.

To support our dietary supplement customers with educating stakeholders about probiotics and the importance of scientifical documentation and clinical studies, we have launched a new online platform in the U.S. called The Probiotic Institute that is targeting both health care professionals and key opinion leaders as well as consumers and the general public.

With regards to our Human Microbiome lighthouse, I am pleased to report that BacThera, our joint venture with Lonza, signed its first customers' contracts, and we are progressing well with setting up the contract manufacturing organization for live biotherapeutic products. By now, most managerial roles are filled with a good pipeline of potential customers from different indication areas, and we are on track to complete the first stage of our CapEx investments to serve the preclinical to Phase II trials by the end of this calendar year.

Looking at Food Cultures & Enzymes. The sales team continued to focus on the commercialization of recent launches and upselling. And in the current environment, we experienced a lot of interest for our solutions that can help drive efficiencies, for example, our cheese enzyme, CHY-MAX Supreme.

In bioprotection, I am excited to share that the team has made a very important discovery on the mode of action of bioprotective cultures that was published in a renowned scientific journal recently. This discovery underlines our innovation leadership in the field and is important for the further development of our third-generation FreshQ, which we expect to bring to market in 18 to 24 months as well as the expansion into new food applications.

In fermented plant bases, we continue to work with an increasing number of customers on the launch of new products to further expand our application expertise in this dynamically evolving space. We recently joined the California-based accelerator, MISTA, which offers food companies, startups and ingredient suppliers a platform for innovation and co-creation.

Lastly, I am really humble and proud that our efforts to work for a better world have been recognized by Corporate Knights again in 2020, this time with a silver medal after we were named most sustainable company last year. More than 82 percent of Chr. Hansen revenues contribute to the UN Sustainable Development Goals, and we are determined to keep pioneering science, for example, in fighting food waste on the overuse of antibiotics and chemical pesticides with the power of our good bacteria.

With this update on our key initiatives, let me move on to the next slide for a deep dive into our regional numbers. Group organic growth in the second quarter was really driven by Americas and Asia Pacific. In Europe, Middle East and Africa, our largest region, Q2 sales were on par with last year and down 2 percent year-to-date. The adverse economic conditions in the Middle East continue to negatively impact our Food Cultures & Enzymes and Natural Colors business. Health & Nutrition declined slightly due to continued weakness in dietary supplements, while Animal Health grew solidly.

In North America, on the other hand, Health & Nutrition delivered very strong growth, driven by both Animal and Human Health, while Food Cultures & Enzymes revenues were on par with last year. And Natural Colors delivered good growth, driven by coloring foodstuffs. In sum, this resulted in a solid organic growth of 70 – of 7 percent for Q2 and year-to-date.

Latin America posted 16 percent organic growth in Q2 and 13 percent year-to-date, which is a positive contribution from euro pricing. Food Cultures & Enzymes continued to grow strongly, supported by our recent CHY-MAX Supreme launch that saw very good uptake with local manufacturers. Natural Colors delivered very strong growth, driven by new customer wins, which led to solid growth for the first half of the year. Lastly, Health & Nutrition declined because of the aforementioned weakness in Plant Health.

In Asia Pacific, sales momentum improved during the second quarter, mainly driven by Health & Nutrition and Natural Colors that grew strongly, while Food Cultures & Enzymes declined slightly. Overall, this resulted in 5 percent organic growth for Q2 and 1 percent year-to-date. If we look at China, the first country that was hit by COVID-19 pandemic, we saw a further deceleration in the yogurt market, as our customers were impacted by the lockdown.

Not only did COVID-19 jeopardize the Chinese New Year sales, but the lockdown also forced manufacturers to temporarily reduce their production volumes during Q2, which was then partly offset by inventory buildups. Yogurt remains a consumer discretionary in China.

And whilst we see signs of renewed interest in probiotic yogurt also supported by the Chinese government and manufacturers are slowly ramping up production again, it's hard to assess the impact at this point in time. And we, therefore, maintain a rather cautious view on this year.

With this, I would like to hand over to Søren for the segment review of the group financials. But before I do that, in light of our communication this morning, as you have seen, we have announced this morning that our CFO, Søren Westh Lonning, will be moving on from Chr. Hansen at the end of the financial year to pursue his career with a privately – private equity-backed company in another industry.

I want to very clearly outline that our collaboration since I joined has been extremely good, and Søren has been a valuable CFO to me, for example, in the recent strategy review process that we are currently finalizing. He will continue to serve on the Executive Board for the rest of his tenure.

And although this is a regretted loss, we will ensure a smooth transition. We will start the process to find Søren's replacement immediately, and I am confident that highly-talented internal and external candidates will find the role as CFO of Chr. Hansen very attractive.

With that, Søren, let me pass it on to you.

Søren Lonning: Thank you very much, Mauricio. And from my part, I'm truly grateful for the opportunities that I've been given in Chr. Hansen. I do believe Chr. Hansen is as strong as ever and with plenty of interesting opportunities ahead. And I can also assure everyone that my departure is not at all grounded in any disagreements or any dissatisfaction and is only motivated by another opportunity that I simply could not pass up on. I want to specifically thank Mauricio as our CEO and the Board of – our Board of Directors for the trust and the confidence that they have shown in me.

With this, please move to Slide 7 for the business review. In Food Cultures & Enzymes, momentum improved in Q2 compared to the previous quarter. Organic growth was 5 percent with a 4 percent contribution from volume and 1 percent from price, including a smaller contribution from euro pricing. Year-to-date, organic growth was 4 percent, whilst dairy end markets continued to track at a low level of around 1 percent globally.

If we look at the performance by product segment, bioprotection and meat cultures grew strongly in the second quarter, while fermented milk, cheese and enzymes delivered solid growth. Probiotics continued to decline, and this is very much a consequence of the weak Chinese market in Q2 that Mauricio just mentioned.

Looking at profitability. The EBIT margin for Food Cultures & Enzymes increased slightly in Q2 as we continued to see scalability benefits from our Copenhagen site expansion come through. And we continue to see potential to further drive efficiency in our production also going forward.

Please move to the Slide 8. In Health & Nutrition, Human Health delivered solid growth, and Animal Health grew strongly in Q2, whilst Plant Health disappointed with a decline in sales. And overall, this resulted in 8 percent organic growth for the quarter. Year-to-date, organic growth of 2 percent remained impacted by adverse order timing in Q1.

In Human Health, momentum improved clearly in the second quarter. This was very much related to a pickup in dietary supplement sales in APAC because of new customer wins and a strong infant formula performance in North America, driven by the launch of the probiotic strain blend for preterm babies.

On the other hand, dietary supplements in EMEA remained challenged because of lower market growth and delayed customer projects. Our infant formula business in APAC faced a high comparable.

Looking at Animal Health. The business continued to grow strongly on the back of improved pharma economics in the U.S. and supported by our recent launch in dairy cattle. But we also saw a strong performance from our swine and poultry segment in EMEA, which benefited from increased demand because of African swine fever in Asia. That said, ag commodity prices have also turned less favorable in the current market environment. We monitor the development carefully, but so far do not expect to see a material impact on our sales performance for the year.

With regards to Plant Health, the quarter came in below expectations. As Mauricio already mentioned, this was because sales momentum in soybean in Latin America was softer than what we had expected. Bear in mind that bionematicides are still a new solution for many farmers, and it takes time to build penetration.

We have taken steps with our partner, FMC, to address the current situation, but it's also clear that Plant Health will not meet its growth targets for the year because of the slower uptake in soybean. However, we do remain very excited about development in sugarcane and the opportunity in the U.S. as well as the long-term journey for this lighthouse, and we will continue to invest in this.

Looking at profitability for the segment. The EBIT margin was up 1.1 percentage point in Q2, driven by cost management initiatives, which more than offset increased R&D spending for Plant Health, whilst year-to-date, the margin was negatively impacted by the lower revenue in Q1.

Moving on to Natural Colors on the next slide, Slide 9. The division reported 1 percent organic growth in Q2 and flat sales year-to-date, as our Natural Colors business continued to be challenged by low raw material prices for carmine and annatto. Excluding the 2 pigments that are hit most by the price declines, Natural Colors would have reported 4 percent organic growth in Q2 and 3 percent year-to-date.

Regionally, the economic climate in Middle East remained very challenging, whereas APAC and LATAM reported strong growth, especially due to new customer wins. Across geographies, the key growth driver for our natural – Natural Colors business remained our premium range of coloring foods, which reported very strong growth.

Looking at profitability, the division was able to maintain its EBIT margin in the quarter and increased it 60 basis points year-to-date, thanks to the lower raw material prices.

Let's now look at the group financial on the next slide, Slide 10. If we start with the cash flow, free cash flow before acquisitions and special items was EUR 41 million year-to-date compared to EUR 8 million last year. The increase stemmed mainly from an improvement in operating cash flow, driven by a favorable change in net working capital, IFRS 16 adjustments, lower taxes paid and higher operating profit.

Cash flow used for operational investing activities was 9.7 percent of revenue, in line with our CapEx plan for the year. Given the current situation where many investors are looking at liquidity and funding risks of company, let me say that Chr. Hansen is in a very good shape and in a strong financial position to handle any potential short-term disruptions or risk related to the current pandemic crisis.

Net interest-bearing debt was EUR 879 million at the end of February, which corresponds to a leverage ratio of 2.1x EBITDA. And do remember, Q2 is where we traditionally see the highest leverage during the year. With our current leverage, we meet our covenants related to net debt to EBITDA and EBITDA to net interest by a comfortable margin.

Also, if we look at the maturity profile of our outstanding bank debt, there are no major refinancing planned for this year or next year. And as a additional fallback, we have more than 2 years free cash flow worth of committed undrawn facilities.

Thanks to our reliable cash generation, we're able to self-finance most of our investments, and we'll continue to invest in capacity, R&D and people as planned. Also, our dividend policy of distributing 40 percent to 60 percent of net income to shareholders remains unchanged.

With this, I would now like to move on to the guidance on the next slide, Slide 11. Based on the business performance of the first half of our financial year 2019/'20, we maintain our guidance for the full year, although subject to higher uncertainty than normal due to the COVID-19 pandemic.

Assuming no deterioration of the situation and no major supply disruptions, group organic growth is expected to be 4 percent to 6 percent with the microbial platform delivering mid-single-digit organic growth. Expectations for Food Cultures & Enzymes and Health & Nutrition are largely unchanged.

We continue to expect Food Cultures & Enzymes to grow significantly above its end market between 5 percent to 6 percent in the second half of the year and with a small positive impact from euro pricing. Natural Colors is now expected to deliver flat to slight organic growth for the year due to continued low raw material prices and an impact from COVID-19.

Group EBIT margin before special items is still expected to be around 29.5 percent. Increased utilization of our Copenhagen production and lower travel activities will have a positive impact on margin, which is expected to be offset by investment into lighthouse projects and other strategic priorities as well as higher freight costs due to COVID-19.

Free cash flow before acquisitions and special items is still expected to be around EUR 190 million, with CapEx slightly above the EUR 139 million that we realized last year, though we cannot rule out that some CapEx projects will be delayed due to the current environment.

Our preliminary long-term ambition for group organic growth until '25 and for EBIT margin before special items and free cash flow before acquisitions and special items until '22 remain valid until further notice.

And with this, I would now like to hand back to Mauricio to talk about the implications of COVID-19 for Chr. Hansen.

Mauricio Graber: Thank you, Søren, for the good review of the group financials. As we said at the beginning of the call, the COVID-19 pandemic has not impacted our Q2 results in a significant way, except for the impact we saw in China. But of course, we will see an impact in the second half of this year, to which extent is very difficult to predict at this point in time. But let me provide you with a few comments to this respect.

First of all, we need to say that as a supplier to the food and health industries, we're in a very fortunate position because these industries are considered essential. And even though we may see temporary disruptions or channel shifts, overall demand is generally very stable also in crisis times.

In the current situation, the health and safety of our employees are absolutely paramount to us, which is why we have instituted a number of guidances across the organization while complying with protocols of global and local health authorities. Many of our employees across the globe are working from home. Whilst for lab and production staff, we have established enhanced safety procedures. I am really proud how the entire organization is dealing with the current situation and remains engaged and supportive of each other to tackle all these new daily challenges.

If we look at our supply chain, I am pleased to report that our production sites are running at normal capacity and meeting customer demands. As you know, our production setup is consolidated with our main Food Cultures & Enzymes site being situated in Denmark, Germany, France and the U.S. So far, we have not seen any disruptions.

What's clearly challenged these days are our global logistics, yet our team has found solutions and alternative routes or means of transportation to get products to customers on time. However, as Søren mentioned, rates for transportation are increasing with lower availability, specifically for airfreight.

If we take a closer look at the end markets and customer behavior, we are seeing that the number of customer across our 3 business segments are securing additional safety inventories to ensure supply continuity and accommodate increased demand from consumers.

Whilst the food service segment is experiencing severely reduced demand at the moment, we see other customers benefit for extra demand that comes from increased home eating and pantry loading. It's also true that we are seeing renewed interest in probiotics, particularly in concepts that support immunity. But we – how all of these short-term reactions will play out across different regions over time is yet to be seen.

More long term, there is the risk that the global recession triggered by COVID-19 may affect demand negatively, especially in emerging markets. If I look at the medium-term implications of COVID-19, I am probably most concerned about the potential impact it may have on our commercial pipeline and innovation activities.

Normally, we visit our customers on a day-to-day basis, business to run trials, advanced commercial projects and codevelop new innovations. In FC alone –

in Food Cultures & Enzymes alone, we have about 100 customer visits per day. With the various quarantine measures and the travel restrictions in place for an undetermined period of time, this, of course, will negatively affect our commercial pipeline and, to certain extent, could also dampen the speed which we can drive new innovations to the market.

Also note that customers in the current environment are naturally much more focused to ensure their business continuity than driving new product launches, and there may be also an impact for less demand for value offering services and stronger focus on cost.

In sum, the uncertainty level related to the current situation is very high, which is also why we decided, together with the Board of Directors, to postpone the finalization of our strategy review in the Capital Market Day until we have more clarity on the medium-term implications of this pandemic crisis. We will continue to monitor closely the situation and address impacts on a continued basis. And we will, of course, also provide an update to the capital markets in case the situation changes significantly.

Until then, please turn to the next slide, Slide 13. We will continue to execute on our strategic priorities as laid out at the beginning of the year. We continue to believe strongly in the many growth opportunities that our technology platform offers. And we will continue to bring innovative microbial and natural solutions to an increasing customer base across food, health and agriculture.

To wrap up with a few key messages, let me say that Chr. Hansen delivered a solid set of Q2 results with an increasing momentum across all 3 businesses and in line with expectations. We maintain our guidance for the year, assuming no major disruptions in our supply chain from COVID-19. In this pandemic crisis, Chr. Hansen, as part of the global food supply chain, has a crucial role, and we are committed to doing everything we can to sustain the functioning of our society and keep employees, partners and customers safe.

We will come back with a new date for our strategy update and Capital Markets Day as soon as the situation allows. Until then, we continue to follow our Nature's no. 1 strategy.

With this, I would like now to open up the call for questions and answers. Thank you.

Operator: (Operator Instructions) Your first question will come from the line of Jonas Guldborg from Danske Bank.

Jonas Guldborg: I'm sorry to hear that you're leaving, but all the best of luck in your future endeavors there. My first question is regarding the uncertainty of delay in your commercial pipeline. When do you expect that it will actually transform into a negative impact on organic growth?

And could you talk a little bit about how much you expected? And will it also mean that we should expect new organic growth in the coming years to be towards the lower end of your mid-term guidance? And maybe also, how much has the commercial pipeline actually contributed to organic growth historically?

And then my second question is on Plant Health. I think I read somewhere that you expect also Q3 to be negative. So what should we expect now for the full year? And what is the lower – slower development caused by, more precisely?

Mauricio Graber: So Jonas, maybe I'll take a few comments and pass it on to Søren. I would say, overall, on the commercial pipeline, obviously, we continue to have our sales organization very engaged with customers, talking with them about the projects on hand, advancing projects that are earlier in the pipeline. But what you can see is what the limiting factor is.

At this point, we cannot visit customers and have test trials at their facilities, et cetera. So I think your question is difficult to predict because it's not normal stake. I think what we will see is a higher demand for our established products and probably a slower progress on some of the new innovation.

Usually, when we work in projects related to innovation in the food ingredient industry, you're talking about projects that take about 18 months for maturity. So it's not an immediate effect, but it's something that we will work hard to continue to mitigate.

Søren Lonning: Yes. And maybe just adding that. So to your question specifically, when it will start to – we don't expect an impact from this in Q3 really. There could be some impact in Q4. And then it will more – it will be more a topic for '21. But to what extent, what it will mean for our guidance for '21, it's way too early to communicate it, also how fast will various countries open up again. And we are – also it's important to emphasize, we're also still winning projects with customers even though we can't visit them physically.

I think when you look to Food Cultures & Enzymes, you can say that we're growing 2 to 3x the end market growth. And that is really driven by our ability to take innovative concepts and go to customers and convince them that it's the right solution for them.

And that is, you can say, that extraordinary growth that is eventually being impacted beyond sort of the market and pricing dynamic. So that's the magnitude of Food Cultures & Enzymes. It's where we have the largest part of that. But we are still win projects, it's important to say, and still progressing the pipe, but it's just impacting the speed by which we can do it.

And then the question on – yes, well, let me start and then Mauricio can chip in. I think what – if we look to the situation that we're in right now is that in many areas, the lighthouse progress as planned. We are still seeing – we are launching in the U.S. We are still seeing very strong sell-out to farmers and uses of farmers in sugarcane.

One segment which is sort of the – that is posing some challenges right now is the soy segment where we've just had the, you can say, the season down in Latin America. And here, we have simply seen a lower sell in to pharma than we expected in Latin America to soy specifically.

And that's the second most important segment that we have at the moment. And of course, that's post trading. I mean as we also alluded to, it's not uncommon that when you are launching new concepts, a new, you can say, solutions to new customer segments that is not a straight line. And we are working on, you can say, it's also a segment that requires a little more attention to demonstrate the benefits of the – of our solutions relative to sugarcane where it's easily available for the farmers.

So it requires a bit more attention from sales and technical support. And this is why we believe that we, in combination with FMC, can lift the game and we can bring this back. But of course, it's a setback this year that we will not meet our growth targets. But we do expect to come back strong in '21, for sure.

Mauricio Graber: I think the only thing I would add to that, Søren, is we have always said that to continue to deliver on the lighthouse, we will need to advance in acreage in sugarcane, expand beyond sugarcane and soybean, an example, and expand outside of Latin America, the U.S. being an example of that. So high level of commitment to our lighthouse for the years ahead.

Operator: The next question comes from line of Annette Lykke from Handelsbanken.

Annette Lykke: Yes. First of all, a question within the infant formula area. We noticed that the a2 milk saw a quite steep increase in infant formula demand in connection with hoarding in the Chinese market, delivering a growth of more than 30 percent in January, March. But as I can see, you have lower sales of infant formula in APAC, and I think you specifically also mentioned China in this respect. So I'm a bit surprised to see that you have not seen this positive effect from hoarding.

Is there a risk that you're losing market share in China? I'm aware of the hard comps, but that is also going for the other companies.

My second question will be, as you alluded to, Mauricio, in connection with the probiotics as an immune stimulate for – and you said that, that – are you expecting that – more of that? Can you say a little bit more color on that? If you expect COVID-19 outbreak to stimulate the consumers' demand?

And then my last question is on the overall full year growth rate. You had a 3 percent growth in the first half of 2019/'20. And this means that for the remainder of the year, according to your current expectations of 4 percent to 6 percent, this is a 5 percent to 9 percent growth in the second half. What will it take you to hit the high end of the range? What are the main swing factor here?

Mauricio Graber: Thank you, Annette. I'll take the first couple of questions around infant formula and probiotics and pass it on to Søren. So on infant formula, first of all, as I mentioned, I think most – you have to remember that we had a strong quarter in China in infant formula last year, so we have the very high comparable. For sure, we heard also and read the increased consumer inventories on infant formula.

I think for us, a lot of that did not reflect in our Q2 that ended in February. Our main growth opportunity in infant formula continues to be the penetration of probiotic use in infant formula. And that, we are very confident that we continue to be a high-growth area because particularly of the higher-quality trend in infant formula. So quite optimistic about that and we expect that we will see some of those growth benefits in the second half of the year.

As far as probiotic (inaudible)...

Annette Lykke: And (inaudible)...

Mauricio Graber: Go ahead.

Annette Lykke: And you did not see a loss of market share in China?

Mauricio Graber: Are you saying infant formula?

Annette Lykke: In the second quarter?

Mauricio Graber: No, we did not see a loss of market share. Obviously, different customers can grow at different pace in a given quarter. And bear in mind that the shelf life of infant formula products is also 2, 3 years. So it's not necessarily that a hoarding in February will hit our financial numbers in Q2, ending end of February in China.

So I would be – caution not to overinterpret it. One segment in one geography in one quarter based on this. We are not seeing a loss of market share. And actually, infant formula is one of the examples where we have continued to see wins with customers even during this period.

Moving on to probiotics. Overall, I think the pandemic crisis has created a lot more awareness about immunity and the benefits of probiotics and probiotics in dairy products, not only in supplements. So what I can mention that we see is, we see a lot of more interest on the end consumer and on the customer side from solutions with probiotics and where the science and documentation of our probiotics have a benefit to the market.

Søren, do you want to comment on the H2 growth and other things?

Søren Lonning: Yes. I think given the uncertainty of the environment that we're in, we actually think that 5 percent to 9 percent is a quite reasonable range to give. Of course, many factors can play into which – where we will end in this range. But if we stay with some of the COVID-19 parameters, what will happen in terms of consumer buying patterns? How will that play out?

How will that normalize? How will the – we have seen some customers building some extra safety stock in this situation. How will that play out rest of the year? How well are we able to progress on our commercial pipeline in this environment? And how long will it last?

Those are some of the key elements that goes into whether we will go in the high end or the low end. And then, of course, there are some also more standard operating things like how will the sale season in Animal Health be? Will it be a good season or – and so on.

So I think there are many aspects that can lean one way or the other. I think we are quite confident that we will have a solid second half of the year, and that's also what's behind the overall guidance for the year.

Operator: Your next question comes from Søren Samsøe from SEB.

Søren Samsøe: First, question in Food Cultures & Enzymes on China and yogurt. We saw last year a trend of switch from chilled yogurt to room temperature yogurt, partly driven by higher food inflation. Has this trend continued or accelerated in this COVID scenario? And do you expect now with a recession kicking in that this will be even more so in second half?

Secondly, on the probiotics in Human Health, especially Europe and North America here. Do you see the trend for online sales of probiotics has increased significantly? And does this give a negative mix effect to you guys?

And then finally, if you could just tell us what has caused the acceleration of the bioprotective cultures in Q2?

Mauricio Graber: Thank you, Søren. I think on China, I probably read and have access to similar information that you have. It's honestly very difficult to predict because there are so many moving pieces. What I could say is the effect we had in China was first that ambient had an impact that we – it was missed the gifting of the Chinese New Year.

So there was definitely a volume loss there that we saw in February. When you look at what's happening after COVID-19, there are many moving parts. On one side, ambient, there was more inventory with customers because it has a longer shelf life. But ambient usually has a wider distribution in the country and the distribution was more challenged in the country.

On the other side, ambient is produced closer to the point-of-sale and what didn't get sold go to waste. So you have a renewal of the demand for chilled. And then on the demand, I think you have 2 conflicting factors. On the positive side, you have the government that has been more vocal on the positive of probiotics and dairy products to build immunity, but you definitely have a consumer base that continues to struggle with the economic situation and the high food price index from the swine situation. So a recession with awareness probably balancing those conditions.

As far as probiotics in the U.S. and online, I don't think that's negative for us. I think our customers rebalanced through the last period. And I think you will see that the demand, whether it's online or retail, will continue to be a positive trend from where we were on probiotic demand.

Søren Lonning: Yes. And you should not expect any negative mix effects from what we see right now in the U.S.

Regarding your third question regarding the bioprotection and what drove that. That, you can say, is we haven't launched new products into this category. So it's more a question of our execution of the commercial pipeline we have of projects with customers where we've seen some good wins that are helping deliver a solid result for bioprotection.

It – we saw it actually playing out a little bit across the different product segments that we have. So we saw a more positive picture across most of our segments be it fermented milk, cheese or meat. So generally, we are pleased with – that we're able to drive the conversion of these solutions with customers.

Søren Samsøe: But can you say more of it? If it's the second generation or the first generation driving the growth? And what regions you're seeing the acceleration happening?

Søren Lonning: Yes. We have actually seen – we have actually several regions doing well, and the majority of the growth is driven by our second generation. I think it's very important to emphasize the second generation is doing quite well. It's driving the far majority of the growth that we are seeing in the category.

It's just not unfolding the full potential that we hoped for when we originally launched it. And that's why we are – have – are accelerating the efforts on third generation. So there should no – be no misunderstanding that the second generation is not selling well and ensuring growth in the market. It is.

Mauricio Graber: And we have also not seen really a large cannibalization between second generation and first generation. So good sustained sales of the first generation and most of the growth, as Søren mentioned, driven by the second generation.

Operator: Your next question will come from Heidi Vesterinen from Exane BNP Paribas.

Heidi Vesterinen: So first, on your long-term guidance, when you talked about potential risks to your long-term guidance, you talked about how the impact on innovation in your commercial pipeline is a little bit unknown at this stage. What about the emerging markets?

That has been a big growth driver for you in past years. Is it not a risk – is there not a risk that we see a sustained slowdown in emerging market growth? So that's the first question, and that's on the back of the virus because it's only just beginning in the emerging markets, right? And I think there could be long-term implications there.

And then the second question, I wanted to ask about how commodity prices impact your business. So for example, if we take dairy, there is an oversupply of milk at the moment. Now that could encourage cheese production, so it could be good for you. But then again, cheese goes into food service, which is not doing well. So net debt, what does this all mean for you?

And also on the Animal Health side, you talked a little bit about this. But you said at this stage, there's not an impact. But going out, I heard a bit about stockpiling of animal feed. But then we're also seeing that meat processing plants are being shut. So could this come and hit you later on? Could you talk a little bit about dairy and animal, please?

Mauricio Graber: So, Heidi, on your first point about emerging markets. For sure, if – as I mentioned in the call, we did not see an improvement in trading conditions in emerging markets, particularly the Middle East and China in Q2. And obviously, that remains our concern also with the information that you're seeing on the growth projections for GDP in emerging markets.

And as we also mentioned, dairy, underlying dairy markets had also at a low cyclical point of growth. So obviously, those 2 are concerns. There's many other opportunities that we continue to drive our business. But for sure, those are, let's say, some of the clouds on the horizon.

Søren, do you want to comment on commodities and Animal Health?

Søren Lonning: Yes. On the commodity prices, I would say, generally, when milk prices go down, it's typically positive for Food Cultures & Enzymes because it's a result of a higher – often the higher milk production that often needs to be stored one way, and cheese is one of those vehicles. So typically, that links to something that's favorable to Food Cultures & Enzymes.

On the other hand, lower milk prices, we have seen that being something that impacts the farmers' ability to buy our product in Animal Health. So normally, there's a little bit of a hitch these ways that plays in that you can't – we can't both do well in both segments driven by this.

But overall, outlook for cheese is quite solid at the moment. When we look forward, I mean, we are still – even though growth is not to the level that we saw 1 year ago, the – you can say, the production levels remain at a quite solid and high level.

When it comes to the Animal Health part, I would say this is a small flag that we have in the horizon that the lower milk prices. How will that play out on pharmaeconomics and influence our Animal Health business, and that's a little bit more uncertain. But it goes into sort of the overall risk balance that we have taken in and applied for the guidance that we have given for this year.

Mauricio Graber: And I think Heidi, just as you mentioned, cheese and food service, it's true. And we see a lot of strength on the other side on grocery. And then you see categories like frozen pizza that have done very well, and all of those use

FC&E cultures for mozzarella cheese that goes in culture. So there's a shift in channels, there's a shift in consumer behavior. But overall, we seem to be performing well during the pandemic shifts.

Heidi Vesterinen: Do you have any idea how much of your sales might go into food service? And is it just cheese? Or is there a dip in colors as well?

Søren Lonning: It is also in colors. We can't – we will not give you an exact number on this. But I can say that the majority of our sales in Chr. Hansen that relates to food goes into traditional food products sold via retail and online.

So that is clearly larger than our food service. It's clear cheese has an exposure, especially North America, less so outside, so in Europe. And then Natural Colors, it has been a focus area also to win business in the food service industry for Natural Colors solutions. But overall, you can say the traditional retail, et cetera, is clearly larger than our food service exposure.

Operator: Your next question comes from line of James Targett from Berenberg.

James Targett: Søren, just from me as well, many congratulations on your new role, and it's a shame that you're leaving us.

My questions are on – just on – firstly, just on the supply chain because you obviously said that your guidance is based upon your supply chain remaining functional. And at the moment, that the – there's been relatively limited impact. Could you just maybe talk about where you see the biggest, where the potentially biggest risks for you lie?

You mentioned transportation, but I'm just thinking in terms of if you break it down into sort of raw material procurement, your manufacturing and then your logistics to and from your customers, where you see the biggest risks?

And then you did also mention your customers were securing safety inventories. I just want to be – we're halfway through your Q3 now, so to what extent do you expect – or are you seeing a benefit in Q3 from your customers maybe stockpiling regions to a certain extent? And how material could that bump to Q3 be, if at all?

And finally, just on – if you look at the demand for your core dairy products, it sounds like the net effect of COVID-19 in China has been negative in your core dairy portfolio. So as we look at the situation spreading globally, just in – amongst your core dairy products, do you think this will be a – in terms of customer – or sorry, consumer demand, do you see this being as a net negative or positive?

Mauricio Graber: Thank you. I'll take part of the questions and pass it on to you, Søren, for some others.

So on your overall question on supply chain, I would say, when you look at raw materials and insourcing or procurement, I think we have a diversified source of raw materials. We have not seen any major risks. And also, we have taken our own measures to ensure that we have safety stocks to be able to manage the demand. But we're always concerned about risk as we are a global company, and we have global sourcing platform, so we – it's a risk, and that's why we flag it.

As far as manufacturing, the key thing in manufacturing is that we continue with the additional safety measures that we have to make sure that we – our employees are healthy and safe to be able to come and work and produce. We have a high automation in our facilities. So our degree of confidence on our manufacturing capacity is high.

Transportation and distribution is a challenge, but we've seen China mainly coming back. And we have seen the transatlantic and transpacific routes to also be available even if it requires more planning and a higher cost. So the guidance we are giving is barring any material disruptions from our customers having to shut down plants or us being on that unfortunate situation. And we cannot bar any of those being a risk.

On the core dairy portfolio, before I pass it to Søren for your comments on Q3. I would say, dairy, I think, has – net-net, I would say, has a benefit. So obviously, we see an interest on the fresh dairy, on yogurt, and particularly on yogurts with probiotics and concepts around immunity. So I think net-net, the shift to grocery and the at-home consumption has been positive for many of the end categories where we sell our core dairy products. Søren?

Søren Lonning: Yes. If I was to comment on your questions related to Q3, I would say that we will not give any specific guidance on Q3. First and foremost, I would say we have seen some customers increasing their safety stock in March, which is positive, you can say. On the other hand, there are also some effects that are impact negatively. You – we talked about our ability to progress our commercial pipeline.

And also extra safety targets, it's very difficult to predict how that will play out in the months to come. So I mean don't – I would be very cautious to give any guidance in terms of that. There will be pluses and minuses from the corona here. And we believe that overall, probably for the year, it looks to be netting out for Chr. Hansen. And I think that's the overall message that we want to leave you with.

Operator: Your next question comes from the line of Faham Baig from Credit Suisse.

Faham Baig: A couple of questions from me. If I could start with the shorter-term dynamics. I appreciate you've kept your guidance for the full year. But at the same time, you've forgone some part health sales that you envisaged. And China turnaround is probably more uncertain than initially expected as well.

What is the offsetting factor, particularly given the uncertainty that this pantry loading you might be seeing in March might easily deload in May or something? So what gives you the confidence to still meet that guidance?

And then secondly, on just long-term growth. Could you give us a few comments on how you're progressing in terms of entering adjacent categories? I think you'd mentioned some plant-based wins and how you see innovation making up that gap between the market growth rate insourcing and the sort of mid- to high single digit growth that you're forecasting in FC&E?

Søren Lonning: OK. So if we look to the shorter-term dynamics, it's true that China in Food Culture & Enzymes was unexpectedly challenging in Q2. And it's also Plant Health, you're absolutely right, that it's coming down a notch below what we expected. Bear in mind, it's not the largest category that we have in Chr. Hansen.

And then there are a few elements that is playing out favorable. We are seeing more interest for probiotics into immune stimulating solutions. And that's an interest at this point in time. We need to see it play out in real sales, obviously, but there is a high interest. We're also seeing Animal Health tracking quite strongly. And although there are some clouds on the horizon now, it looks to be a very strong year in Animal Health.

And then I would say the core offering in Food Cultures & Enzymes of our traditional cheese, fermented milk, meat, et cetera, just continues to perform very solidly and have actually done so during the many quarters we have seen. So those are some of the areas which are performing quite solidly. And they are larger than the other areas, and hence, we don't need to overperform so much in these to compensate. So that was a few elements to that one.

In terms of the longer-term growth outlook, I would say that even though we are not out announcing a new strategy, we continue to execute on Nature's no. 1 and that also includes plant-based. I mean it was already something that we were working on before. And we are seeing good progress. We are winning projects. We have a very healthy pipeline and we'll continue to move ahead according to our Nature's no. 1 strategy in that area.

And I – generally, I think the growth opportunities that we have under the Nature's no. 1 strategy are quite clear and quite attractive for us. So we will just continue to working on executing to the best of our ability in that areas. Mauricio, maybe you want to add something here.

Mauricio Graber: Yes, and just to provide a little bit of a positive lens on that. If you look at COVID-19 and the impacts on society, I think there will be a young generation that has a lot of interest in biosciences. I think we will see more talent coming into our industry, interested in innovation.

I think the spaces where we work, quite honestly, whether it's in Food Cultures & Enzymes, developing new technologies for dairy and probiotics and cheese, will be more relevant as we come out of this pandemic and also in – for our Animal Health and Plant Health business.

So I think we see a strengthening of the interest and the opportunities in the areas where we work as we think about what will be some of the social drivers when we come out of it. For sure, you will have the economic conditions that are likely to be challenging. But I think the long-term prospects for Chr. Hansen are quite strong. And that's why I have stated that I have confidence that we will manage well through the economic crisis.

We have a strong focus on the safety and well-being of our employees, understanding the supply side, managing the demand side with our customers, and together with Søren, staying very focused on our liquidity and cash flow. So confident on the long-term growth.

I think we have time for one more question.

Operator: Your next question comes from the of Patrick Rafaisz from UBS.

Patrick Rafaisz: Just 2 quick ones, please. The first is a follow-up on the plant-based dairy commercial projects. Any chance you could quantify these commercial opportunities in the near or the mid- to long term?

And then the second question on Natural Colors. Already about 6 months ago, you were starting to talk about carmine and then also pricing looking close to rock bottom. How – what has changed? Has anything changed? Do you see maybe some price improvement potentially in the near term? Or do we still have to wait for that to happen?

Mauricio Graber: So on plant-based, I think we released an exciting communication today as well that we're joining MISTA, the California-based co-creation with – together with other exciting partners. And I think it shows how we believe that fermentation in Food Cultures & Enzymes and our technologies will play a key role in plant-based. We will not give you a specific number, but we're working with a large number of customers in a large number of projects.

One of the things that we have seen though, through COVID-19, and it has been widely commented in the reports, is that really strong brands with strong distribution have done well. So we have seen a little bit of delay in some of the launches of our plant-based products or new activity in that space.

As it relates to Natural Colors, I think, Søren, before I pass it to you, we have said that both carmine and annatto have been already, since Q1, at historically low prices, and they had largely remained at or slightly below those historically low prices. So we have not yet seen a change in the pricing for those pigments.

Søren Lonning: Yes. So I mean we did see – we have seen a declining trend. It came it came down during Q1. We thought that was the bottom. It took a small notch down, further, actually. So a level I haven't seen before with $12 per kilo. And now we believe that is truly the rock bottom. But more importantly, I think, is to consider that one thing is what the raw material impact is and where it is, but it takes some time before it translate into our top line.

And exactly forecasting what the impact will be is due to the dynamics in the industry and all that. And that's where we can see a more negative impact from that also. But it is the lowest price point I've seen in my 13 years in Hansen for carmine. So I really do believe that this must be the bottom, and prices will, over time, normalize to a more stable, reliable level.

Mauricio Graber: I think the exciting part of Natural Colors is that we've seen FruitMax, which is, let's say, our higher-end coloring from foods perform very well with double-digit growth. And obviously, that also translate into the positive profitability development that you have seen for the Natural Colors division.

Søren Lonning: And bear in mind, one thing is that the impact on the top line from raw material prices, our EBIT margin is developing favorable because it's more top line than it's a bottom line topic when you have these movements in raw material prices. I think that's also an important point to bear in mind for Natural Colors.

Mauricio Graber: OK. Thank you very much. I think that was the last question, so we will end call. Thank you, everybody, for participating in the call, for your interest. Stay safe and we will come back here and comment whenever we will set a new date for our Capital Markets Day. Until then, thank you very much.

Operator: That's conclude the conference for today. Thank you for participating. You may all disconnect.

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