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Haypp Group

Q2 2023



Prepared Remarks

Welcome to the Hyatt Group Q2 Report 2023. For the first part of the conference call, the participants will be in listen only mode. During the questions and answer session, participants are able to ask questions by dialing Now I will hand the conference over to the speakers, CEO, Gavin O'Dowd and CFO, Peter Delli. Please go ahead.

Thank you very much. Thank you. Good morning, everybody, And welcome to Hyatt Group's presentation of our interim report for the Q2 of 2023. Today, we will briefly walk you through an overview of our business and comment on the operational and financial performance for the Q2. The interim report and the results presentation is available at the Investor Relations section of our corporate website.

Presenting today, in addition to myself, is Peter Deli, our new CFO. During Q2, Svante Anderson, our previous CFO, moved to a new role of Chief Operating Officer in the company. With that, I would like to pass over to Peter to introduce himself.

Good morning, everyone. It's a great pleasure to be here and support Haag Group to achieve its long term goals. By the way of introduction, I'm looking for Haag Group since 2020. While Evidence 1st was busy with the IPO, I guided the business to achieve its financial objectives. Prior to life, I accumulated a substantial amount of category knowledge during my 7 years with BAT, while prior to it, I worked for Ambrecht in a retail environment the consumer focus and margin management was essential.

What you can expect from me is straightforward. I will ensure that we keep the right balance between profitability and growth, we will keep investing in a smart way, while I will emphasize cash generation. With that, I'll give it back to Gavin. Thank you, Peter.

Moving to Slide 4 in our results presentation. Here we state our higher purpose of inspiring healthier enjoyment to millions, which is predominantly moving people from cigarettes to safer alternatives, Which was traditionally SMUS, but in more recent years has been nicotine patches. On Slide 5, we have a chart presenting the spectrum of nicotine products and their relative level of harm versus cigarettes. Pipe Groups primary focus on nicotine patches and snus lies at the lower end of the spectrum. The scientific body of research around modern harm reduced alternatives to cigarettes has come a long way in recent years.

In addition to nicotine patches and snus, products such as tobacco heated devices and vapor are widely accepted as carrying a significantly lower level of harm traditional cigarettes and other tobacco smoking products. On Slide 6, we can see what smoking rates are like across a range of European countries. Sweden, with a strong tradition of oral nicotine and robust harm reduction strategy, it's below 1 third of the European average of smoking rates and is on track to become the 1st smoke free country. In Norway, where oral nicotine products were introduced some 20 years ago, smoking rates are at a similarly low level at Sweden. On the right hand side, we can see how smoking rates collapsed between 2,005 and 2020 in Norway, especially among the younger part of the population.

And it is almost perfectly correlated between that and the uptake of nicotine patches and snips among the same age groups. It is this impact on public health which we wish to bring to other countries. Turning to Slide 7. We can see the outlook for the market, which we laid out in 2021 in connection with our IPO, And we believe it is equally valid today. We see a global market size for nicotine patches and snus, which will increase from €27,000,000,000 in 2020 to €60,000,000,000 in 2025.

All of this growth is going to be driven by nicotine pouches, which will increase from share of the market of 30% in 2020 to 80% in 2025. Since this market outlook was prepared, nicotine patches has been tracking in line with the expected CAGR. The category is now growing faster than initially expected. Hyatt Group is growing significantly faster than the category in each individual market. The primary driver behind the growth of the category is strong consumer demand for less harmful products, which is greatly supported by regulators in general Adapting the principle of harm reduction into their legislative approach to nicotine products.

This in turn has led to a significant investment in the category from other industry players, both in large tobacco companies and many credible new entrants who are driving innovation. Furthermore, the category is very well suited for online and we see online penetration rates increasing for every quarter that goes by and we expect online to increase at healthy levels. Moving along to Slide 8. You will see an overview of our logistics infrastructure. Convenience remains one of our key USPs and the ability to offer our customers across all markets, fast and reliable delivery sets us apart.



We completed the 2nd phase of our warehouse expansion plan in Q2 of last year and we're now operating 6 warehouse locations across our core and growth markets. We have managed this expansion while continuing to maintain healthy inventory turnover of 15 tonnes. Furthermore, the warehouse expansion has led to a further improvement in customer retention rates as the convenience levels have increased. During Q3 of this year, we plan to open our own warehouse in Milton Keynes, which is just north of London. We also plan to refurbish our Stockholm warehouse in Q4. In addition, we are progressing to another phase where we are enhancing our infrastructure and our back end.



In addition to supporting scalable future growth in our current categories, it would also enable us to efficiently move into new categories into new markets and adjacent categories. Moving along to the operational highlights for Q2 on Slide 10 and starting with our performance in nicotine pouches. The growth in consumer demand for significantly less harmful nicotine products remained strong in Q2. All growth for the combined nicotine pouches news category is coming from nicotine pouches. With this in mind, nicotine pouch volume is our primary measure of growth.



In addition to the general nicotine pouch growth category growth, Hyatt continues to grow market share across all of our markets. Our nicotine pouch volume increased by 35% year on year for the group, driven by solid growth across all our geographies, we are delighted to say that nicotine patches are now more than half of our volume for the first time ever. We continue to play a pivotal role in launching products in the nicotine patch category, which in turn accelerates the migration from cigarettes. During Q2, over 20 percent of our nicotine patch volume relates to products which were launched in the past year. As I briefly mentioned earlier, our investment in logistics infrastructure in the second half of twenty twenty two have resulted in material improvements in customer satisfaction and retention rates.



In a difficult macroeconomic environment for our customers, we are particularly pleased to note that we are growing our active customer base by 18%, indicating that our value proposition remains highly relevant even in challenging economic times. On Slide 11, we will look at some of the regulatory updates. The Norwegian Parliament voted in the beginning of June in favor of a new national tobacco strategy. The public health strategy comprises of measures within most of the priority focus areas for the Norwegian Health Policy and is renewed every 4 years and includes a national strategy for the tobacco control, the proposed measures should be seen as a gross list of efforts based on previous input from different health organizations. The public size measures is not a legislative proposal, but a formulation in the strategy with the aim to prevent minors from gaining access to tobacco products and based on previous public health strategies, it's clear that far from all of these desired measures are being realized.



While we share the government's view that the issues addressed in the public health strategy, we do see that domestic online channel is already being fully committed to preventing youth access to nicotine products through robust and modern age verification processes. Our own age verification process has a zero failure rate preventing underage buying from our e-commerce stores, which is unheard of in any age verification measures in physical stores. Hence, a ban on domestic e-commerce is unlikely to be part of a solution for youth prevention. It was clear during the Norwegian parliamentary hearing the majority of members did not support an online ban. On the back of this, we remain confident that legislation will continue to support domestic online sales.



In addition, on the 30th June, Sweden introduced more rigorous product standards for nicotine patches. We welcome this legislation, which brings the rest of the Swedish market broadly in line with Hyatt Group's own internal product standards. With that, I'll pass the word over to Peter for comments on the financial performance.



Thank you, Gary. Let's move to Page 12 and the financial overview for the group. In Q2, we reported a net sales increase of 23% in the 2nd quarter. In constant currency, net sales increased also by 26%. Effectively, all of our growth is attributable to our progress with nicotine pouches, and we are recording solid growth rates for nicotine pouches across all markets, while tobacco based sales revenue is only growing low single digit.



The gross margin improved year on year by 0.4 percentage points to 12.9%. Which corresponds to an adjusted EBIT margin of 2.7%, up by 0.4 percentage points versus last year. The drivers behind the EBIT margin uplift is higher volume and gross margin partially offset by higher adjusted OpEx from investment. The organization support further growth. Cash flow from the operating activities during the period amounted to SEK 130,000,000. Going to Page 13, where you see an overview of our core markets.



Reported net sales for the segment grew by 12% during the quarter and amounted to SEK 587,000,000. In constant currency, net sales increased by 14%. Sweden nicotine pouch is continuing to perform well, while the market decline in smooth consumption partly driven by migration to nicotine pouches has negatively impacted the overall performance of the market. In Norway, we are very pleased to note that net sales continues to increase at healthy levels. Our nicotine pouch volume in the core markets grew 25% with both Sweden and Norway showing strong performance.



Our smooth volume declined in Sweden less than the market, while in Norway, we achieved a low single digit growth. Looking at the profitability, For our core markets, it remains strong. On the last platform basis, we have generated SEK 185,000,000 of EBITDA in our core markets. The EBITDA margin was 7.7 percent in the 2nd quarter, 0.6 percentage points down versus last year. The market reduction in the quarter is attributable to the Insight's revenue phasing.



We always look at the Insight as Strategically important element of our business. The demand from our business partners for insights has become more strategic in nature. These projects are often completed over a longer time frame and recorded when completed. During Q2, we had several projects underway but not completed. We will finish this project in Q3.



Now let me move to our growth markets on Page 14. Reporting net sales increased by 78 percent to SEK182 1,000,000 for the 2nd quarter and in constant currency net sales increased by 70%. We had strong performance particularly in the U. S. And U.



K, and we see continuous acceleration for growth rates. Our nicotine pouch volume in the gross markets increased by 55% in the quarter. EBITDA amounted to a negative SEK1 1,000,000 versus negative SEK 18,500,000 during the same period of last year. The improvement is driven by volume growth and looking economics of scale. On Page 15, instead of just looking at the last quarter, I would like to view stable performance over the last 6 quarters.



The graphs are showing what quarter over quarter sales growth in percentage broken down by the key elements of it, organic performance, acquisitions and foreign exchange impact. As we talked about until the end of Q3 last year, the group sales performance was hindered by Norway. However, starting with Q4 2022, our sales growth great sales growth recovered. In 2023, We grew more than 20% in both quarters and this growth was fully driven by organic performance. Core market sales remain robust Despite our substantial channel share, we are extremely happy about our growth markets where sales growth accelerating And reached 70% in constant currency in Q2.



Now turning to Page 16. I would like us to focus on the adjusted EBITDA trajectory of our growth markets. Be aware And we always be committed to support the growth of these markets. However, with the gradual improvement quarter over quarter, we believe that we are only a few quarters away to achieve profitability in this business segment. On Page 17, we have our selected KPIs.



We achieved a 6% increase in our average order value, while our average order size remain constant. I would like to focus on this slide more on the balance sheet in particular. Our financial position remains strong. We closed the quarter with a net working capital position of SEK157 1,000,000, out of which our inventory accounted for SEK 149 1,000,000. The excess inventory we build up ahead of the exercise that CNC is in orbit was successfully sold out during the quarter.



The fast moving nature of our We sold out during the quarter. The fast moving nature of our products naturally implies high inventory turnover rates, And we are continuing to seize opportunities for inventory loading as they arise going forward. Net debt increased to SEK110 1,000,000 corresponding to a net debt to adjusted EBITDA ratio of 0.9 versus 1.8 times in full year 2022. With that, I hand the word back to Geron.



On Slide 19, we reiterate our long term targets of CHF5 1,000,000,000 in net sales by 2025. We also reiterate our profit target of high single digit adjusted EBIT over the medium to long term. As you will have seen from Peter's material, we are already rapidly closing on this target in the core markets. And as you have also seen, the growth markets are rapidly moving to profitability, And we expect them to be net contributors in a few quarters' time. During the due to the growth potential in the category, The Board does not intend to issue any dividends in the foreseeable future and instead utilize our strong cash variation and robust balance sheet to accelerate growth.



On Slide 20, we highlight the potential of which we see for the overall category growth and also the potential for online to take larger share of this category, given how suitable the characteristics of the category are for online. We also reiterate our market leading positions in all of our key markets. Moving along to Slide 21 and our current trading. Market trends for our harm reduced products remains favorable, and we continue The transition of the business into being mainly driven by the nicotine parts category. On top of that, the online channel continues to grow relevance in the category.



In terms of inflationary pressures on inbound costs, we reiterate our previous guidance that inflationary pressure on our cost Given the non cyclical characteristics of the category, we remain confident that any inflationary pressure can be passed on. Looking ahead, the increase in growth rates, which we saw in Q2, has accelerated at the start of Q3. Yes, we need to be conscious that this could be at least in part driven by favorable weather conditions. We recognize That a significant number of nicotine pouch users in the UK were or potentially still are vapers. The broader portfolio not only gets us a foothold in the vape category, but helps our customers to migrate to nicotine vouchers.



Our capabilities to attract new customers and retain them with our offering, hinge around convenience, assortment and price continues to perform well in the current macroeconomic environment. We are on track with our plans to enhance our digital infrastructure, including our back end, enabling further growth opportunities, both in terms of new geographies and new categories in addition to releasing benefits of scale. And lastly, we are very well positioned in the current complex Economic environment for consumers with a strong balance sheet and a non cyclical product and the capital light business model, We remain highly flexible and to strengthen our market positions. As a wrap up, I would like to guide you to Slide 22. There's more than 1,000,000,000 smokers in the world, the majority of whom are looking for healthier alternatives And nicotine pouches is the fastest growing category.



The category is perfect for online and we are an undisputed global online market leader We have over 10 times the size of our nearest competitor. We have a symbiotic relationship with our suppliers. In addition to being the partner of choice for uLogist, are also the largest provider of consumer insights. We continue to welcome proportionate regulation and we often benefit from it And our unit economics continues to improve as we scale. We have a highly engaged team with core competencies across both Nickelodeon Industry and E Commerce.



Before I hand over to the operator for questions, I would like to invite you to our Capital Markets Day in November in Stockholm. Operator, now I would like to open the line for questions,

Q&A



The next question comes from Nicholas Ekman from Carnegie. Please go ahead.



Thank you. Just a couple of questions from my end. Firstly, if you could elaborate a little bit more on the regulatory in Norway, what do you think is the most likely process in the coming months or quarters? How lengthy a process do you expect this to be before we get some clarity on what the parliament's intentions are for this the proposed online ban?



Absolutely. Good morning, Nicholas. So I guess just to give a little bit more background within that regulatory space, The initial concern that hinged around some of this within Norway was a slightly broader aspect than online sales. It hinged a lot around Digital marketing such as TikTok and it also hinged on the basis of some illegal products being sold cross border online into Norway. So our understanding is that the Norwegian regulations are becoming much more familiar with the real problems that they're dealing with at this point in time And that they are starting to recognize to differentiate for what the better term perhaps the goats from the sheep a little bit on this space and determine where these fundamental problems are within this category.



So as we're identifying that, it could alter the timeframe a little bit on how long it takes for this to come through. There is different ways that this can be brought back and can be brought into legislation from here. And it's difficult at this stage to determine exactly which path they're likely to go on. But we envisage that we would We know a lot more in the latter part of this year.



Very clear. Thank you. And then can you just repeat, I didn't quite catch. You talked about in the Nordics, the growth rate. What was the difference between Sweden and Norway in this quarter?



Yes.



So we saw very strong performance in both markets over this quarter. Of course, Norway itself had come from some more difficult times back in Late 'twenty one early 'twenty two, we see it returning back towards normalized growth. And we don't break out the market Specifically, but what we can say is there's not a fundamental difference in the growth rates across both markets. And nicotine patches of the drop Both, across both markets entirely.



Okay, okay. Clear enough. On your growth target, This SEK 5,000,000,000 in sales by 2025, I think from here that requires a growth rate of 25% over the next two and a half years, Which is a lot more than you've achieved in previous quarters. And now, of course, growth has accelerated in Q1, Q2, and you talk about a further acceleration In Q3, do you think it's feasible for growth rates to stay around or to accelerate and stay around 25% In the next two and a half years, is growth in growth markets expected to be strong enough to keep a growth rate at that level?



Perhaps maybe to give a little bit of context around this, what we have seen when it comes to the overall category in general That of course, the category is getting in towards a substantial share of nicotine sorry, and I'm talking about nicotine pouches here, is getting into a substantial share of The overall oral category for within Scandinavia. However, what we see is the nicotine patch category is accelerating in growth In the growth markets and particularly within the U. S. Where we see the category showing very robust growth, it had Been slowing down a little bit during 2021 2022, but with some very strong performance market wide over the last 2 to 3 quarters, which continue to accelerate. So I feel as though there's a very strong tailwind around the overall category.



And of course, we continue to see Growth of online as a share of the markets across each of these markets. So we feel as though a lot of the dynamics for Robust growth going forward are very much in favor.



Good. And can you tell us Roughly what the online penetration of nicotine pouches is in the U. S, do you have a rough estimate of what that could be?



The definition of online in the U. S, I guess, is a little bit skewed. But if we take it because there are some Cross border sales going into the U. S. Via sort of a gray market here along the way.



But if we take a look at the domestic market, We envisage that online is operating somewhere between 3% 4% of the online market at this point in time. And we are by far the largest player Within the domestic within the entire U. S. Market. So we see strong growth potential within it.



Very clear. Hi, Carlos.



Hi, Carlos. Hi, Nicolas. Maybe just connecting that point back to the previous question which you'd asked. I think it's perhaps also worth noting that as we see a growth in the category, there is often a delay factor between people moving into the category And people moving into online. So we feel as though that's sort of positive Progress that we've seen in the category over the last 2 to 3 quarters, we envisage will inevitably spill over into online as people become more familiar with the category and alternative ways that we



Thank you. And then just a final question. You talked a bit here about profitability in the growth markets You will be EBITDA positive even including a potential acceleration of the rollout?



No, this is very much hinged on the existing markets which we're within. And we've taken the opportunity in November when we do the Capital Markets Day To give a little bit more color on what our expansion plans will be going forward.



Clear enough. Thank you so much for taking my questions.



Thank you, Nicholas.



The next question comes from Andreas Lundberg from SEB. Please go ahead.



Thank you. Okay, can you hear me?



Good morning, Andreas. How are you?



Good morning, I mean, I'm good. Just a few ones here. You talk about some investments, both to make sure you can Moving to new markets, new categories and so forth. What does this mean on your investments or costs



Yes. So what we're doing is we're Very much ramping up our back end infrastructure, our ERP systems, our transport administration, our API is connecting all of our systems together, our warehouse management systems, etcetera. So we're grouping all together here to be able to be much more scalable as it goes forward.



When it



comes to our cost base over the medium term, one of the benefits we see with this is that the business becomes much more scalable And becomes much more efficient as we grow across multiple categories and multiple markets. So over the longer run, we think this will have quite a positive impact On our operating margins. And I guess the other question perhaps I can get here is what does it mean regarding our CapEx? And I think when it comes to our CapEx, we remain committed to the 1.5% to 2% guidance that we gave as a percentage of sales over the longer term. However, we would also like to highlight that there will be this is not a flat piece.



There will be quarters Which is significantly above and quarters which are significantly below. For example, you can see in Q1 and Q2 and second here, if you see a differentiator, You'll see in Q1 and Q2 that we have been coming in at the lower end of that range. And there will inevitably be quarters where we'll be coming in At the upper end of that range or even above that range, but we remain committed to the guidance that we gave over the medium to long term of



that space. That's correct, Gavin.



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could that be



On the



P and L side, I don't think it will have a negative impact over the short term short to medium term, and I believe it will have a beneficial impact over the medium to long term. Got it. And when you



talk about adjacent categories, What could we expect or what?



Well, we remain committed to our vision of harm reduction. So we would only work with any products which we can confirm are below 5% the harm of the cigarettes and are very constructive in moving smokers away from cigarettes into this space. And this is part of the reason why we have piloted The vape category in the UK at the beginning of this year and when we extended that pilot across to Sweden on one of our stores in the beginning of the summer of this year.



Cool. And lastly, on this, you took Onetime cost for the warrant program, CHF 14,000,000, I think it was. What program was that? And when is the next



Yes. So this program was a bit of a tidy up on a few aspects around the IPO. So it was a program that we released in the AGM in the Q2 of 'twenty three. And because of some historical factors, there was a need to do a tidy up within us, and hence, we took this one as a one off. However, we don't necessarily envisage that this is something which will be done on a recurring basis.



Okay. Thank you so much.



Thank you, Andres. Thank you all very much for your time today. Greatly appreciate it. We look forward to Speaking to you for the update at the end of our Q3 results in early November. And soon after that, we will be following it up with the Capital Markets Day on