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Haypp Group

Q1 2023



Prepared Remarks



Welcome to the Haight Group Q1 Presentation for 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 Please go ahead.



Good morning, everybody, and welcome to Hyatt Group's presentation of the interim report for the Q1 of 2023. Today, we will briefly walk you through an overview of our business I'm confident on the operational and financial performance for the 1st year. 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 Fante Anderson, our CFO. Moving to slide 3 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 that traditionally was snus and in more recent years nicotine patches. On Slide 4, we have a chart presenting the spectrum of nicotine products and their relative level of harm versus cigarettes. Heilig Group's primary focus on nicotine patches and snus lies in the lower end of the spectrum. The scientific body of research around modern harm reduction alternatives to cigarettes has come a long way in recent years. In addition to nicotine pouches and snus, products such as tobacco heating devices and vapor are widely accepted as carrying a significantly lower level of harm than traditional cigarettes and other tobacco smoking products.



On Slide 5, we can see that smoking rates for smoking rates are likely across a range of European countries. Sweden with a strong tradition of oral nicotine and robust harm reduction strategy is below 1 third of 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 similarly low levels to Sweden. On the right hand side, we can see how these smoking rates collapsed between 2,005 and 2020 in Norway, especially among the younger part of the population, And there is no almost perfect correlation between that and the uptake of nicotine pouches and snus among the same age groups. It is this impact on public health, which we wish to bring to other countries.



Turning to Slide 6, we can see the outlook for the market that we laid out in 2021 in connection with our IPO, which we believe is equally as valid today. We see a global market size for nicotine pouches and snus which will increase from SEK27 1,000,000,000 in 2020 to SEK60 1,000,000,000 in 2025. All of this growth is going to be driven by nicotine pouches, which will increase from the share of 30% in 2020 to 80% in 2025. Since the market outlook was prepared, nicotine patches has been tracking in line with expected CAGR of 41% per annum. It is also worth noting that Hype has been growing at a significantly faster pace.



The primary driver behind the growth of the category is strong consumer demand for less harmful products, which is Reported by regulators in general adopting a principle of harm reduction in their legislative approach to nicotine products. This in turn has led to significant investment in the category from industry players, both large tobacco companies and many credible new entrants driving innovation. Furthermore, the category is very well suited for online and we see online penetration rates increase in every quarter that goes by And we continue to expect online to increase at healthy levels. Moving along to Slide 7, you will see an overview of our logistics infrastructure. Convenience remains one of our key USPs and the ability to offer consumers Across all markets, fast and reliable delivery sets us apart.



We completed the first phase of our warehouse expansion plan in Q2 of last year and we are now operating 6 warehouses across our core and growth markets. We have managed this expansion while continuing to maintain healthy inventory turnover of 15 times for 2022. Furthermore, the warehouse expansion has led to further improved customer retention rates as the convenience levels have increased. Having successfully completed the first phase during Q2 of last year, we have progressed to another phase where we are enhancing our infrastructure and backend. In addition to supporting scalable future growth in our current markets, it will also enable us to efficiently move into new markets and adjacent categories.



Moving along to the operational highlights for Q1 on Slide 9 and starting with our performance in nicotine patches. The growth in consumer demand for significantly less harmful products remained strong in Q1. Effectively, all growth For the combined nicotine pouch and snus 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 category growth, Hype continues to grow market share across all of our markets.



Our nicotine pouch volume increased 41% year on year and is just over 100% or in a 24 month basis for the group, driven by solid growth across all of our geographies. Nicotine pouches now account for 45% of the group volume as compared to 37% for the Q1 of last year. We continue to play a pivotal role in launching products into the nicotine patch category, which in turn accelerates the migration from cigarettes. During Q1 22 percent of our nicotine patch volume related to products which were launched in the past year. As I briefly mentioned earlier, our investment in the logistics infrastructure in the first half of twenty two Have resulted in material improvements in customer satisfaction and retention rates.



In a difficult macroeconomic environment for consumers, we are particularly pleased to note We are growing our active consumer base by 21%, indicating that our value proposition remains highly relevant even in challenging economic times. On slide 10, we are highlighting key regulatory developments. In general, we continue to see governments adopting the principle of harm reduction as a core pillar of the regulatory strategy. In Sweden, for example, new legislation came into effect from the 1st August of last year, which clearly reflects this perspective. In Europe, we are also noting Growing governmental interest for harm reduction and we remain positive that the EU will introduce positive regulation for nicotine patches in GBD3.



In a world first initiative in the UK, 1,000,000 smokers will be encouraged to switch from cigarettes to vaping through a Swak to Stop scheme. This effort aims to improve public health and reduce smoking rates. As part of the scheme, nearly 1 in 5 smokers will receive a vape starter kit along with the behavioral support to help them quit smoking. This measure is one of several aimed to helping the UK government achieve its goal of becoming smoke free by 2,030, Which would mean reducing smoking rates to 5% or less. In Q4 of last year, California imposed a ban on flavored nicotine products sold in physical retail locations, which prohibits brick and mortar retailers and vending machines From selling flavored products, while we as an online retailer have benefited greatly from this, it is our opinion that the law to some extent is a step back in terms of harm reduction as it does not distinguish between harm reduced As we have seen other examples of flavor bans, none of which have had any material impact on consumption.



Now that we do expect this type of regulation to in March, the Norwegian government presented a new public health strategy, which expresses the government's desire to ensure better control over the sales of vapes and tobacco products. The government health strategy includes measures within most of the priority focus areas in the Norwegian Health Policy and is renewed every 4 years. The proposed measures should be seen as a gross list of efforts based on previous input from different health organizations. The publicised measure is not a legislative proposal, but a formulation of strategy with the aim to prevent minors from gaining access to tobacco products. Based on previous public health strategies, it is clear that far from all desired measures are going to be realized.



We share the Norwegian government's view on the issues addressed in the public health strategy. However, we do not see a ban on e commerce as part of the solution. On the contrary, e commerce players in Norway, including ourselves, have far more robust procedures in place for preventing minors from gaining access to tobacco products. From here, it's a relatively long process with significant unknowns. We do not know if online sales will be prioritized by the government and if so, what the exact definition of online sales will be.



With that, I'll pass the word to Sante for comments on our financial performance.



Thank you. With that, let's flip to Page 11 and the financial overview for the group. We reported a net sales increase of 22% for the group in the Q1. In constant currency, net sales increased by 21%. And effectively, all of the growth is attributable to our progress within nicotine pouches, and we're recording solid growth rates for nicotine pouches across all markets, while tobacco based volume is only growing low single digit.



The gross margin improved year on year by we continue to further strengthen our position in the value chain within the category, which along with scale benefits in our operations will continue to drive our gross margin performance over time. Adjusted EBIT for the quarter grew by 29% versus last year and amounted to SEK 18,000,000, Which corresponds to an adjusted EBIT margin of 2.3%, which is up by 0.1 percentage points versus last year. And the drivers behind the EBIT margin uplift is higher volume and gross margin, partially offset by higher adjusted OpEx from investments that in the organization to support further growth. Cash flow from operating activities during the period amounted to SEK92 1,000,000. And turning to Page 12 and our core markets.



Reported net sales For the core market segment, grew by 14% during the quarter and amounted to SEK616 1,000,000. In constant currency, net sales increased by 15%. Sweden continued to perform well with an above 20% year on year growth rate, predominantly driven benefit in pouches. In Norway, we are very pleased to note that net sales continues to increase at healthy levels sequentially and on a year on year basis, we recorded a low single digit growth despite inflated comparables in Norway from Q1 of last year, driven by the final COVID lockdown. Our nicotine pouch volume in the core markets grew at a healthy 32%, with both Sweden and Norway showing strong performance, while our snus volumes were flat.



In terms of profitability for our core markets, it remains strong and continues to increase. On an LTM basis, we have now generated SEK 184,000,000 EBITDA in our core markets. In the Q1, the EBITDA margin increased to 8.2%, up by 0.6 percentage points against last year. And the margin uplift in the quarter is mainly attributable to a higher gross margin partially offset by OpEx investments. Moving on to our growth markets on Page 13.



Here, we reported net sales sorry, here, net Reported net sales increased by 67 percent to SEK166 1,000,000 for



the 1st quarter. And in



constant currency, net sales increased by 55%. We had strong performance mainly in the U. S. And the UK. And as Gavin mentioned earlier, we have benefited from the flavor ban in California, which limits the flavor assortment in Physical retail and have led to a strong online migration across the consumer base in the state.



In Europe, we're seeing continued strong demand for harm reduced Products and the U. K, in particular, is showing strong growth, albeit from low days. Our nicotine pouch volume in the growth markets increased by 60% in the quarter. The EBITDA amounted to negative SEK 20,000,000 versus negative SEK 18,000,000 during the same period of last year as a result of continued commercial investments for growth. On Page 14, we have our selected KPIs, and I would like to focus here on the balance sheet in particular.



Our financial position remains very strong. We closed the quarter with a net working capital position of SEK178 1,000,000, Of which our inventory accounted for SEK194 1,000,000. The excess inventory we built up ahead of the excise tax increase in Sweden was successfully sold out during the quarter. At the same time, we took advantage of inbound price Increases in Norway effective from February and built up excess inventory of which part was still to be cleared out as per the end of this quarter. And the fast moving nature of our products naturally implies high inventory turnover rates, and we will continue to seize opportunities for inventory loading as they rise going forward.



The net debt decreased to SEK140 1,000,000 versus year end And with that, I'll hand the word back to Kevin.



Thank you, Sante. Moving along to Slide 16, we reiterate our long term targets of CHF5 1,000,000,000 net sales by 2025 predominantly through organic growth. We also reiterate our profit target of high single digit adjusted EBIT over the medium to long term. And as you will have seen from Svante's material, we are rapidly closing on this target in our core markets. Due to the growth potential in the category, the Board does not intend to issue any dividends for the foreseeable future and instead utilize our strong cash generation and a robust balance sheet to accelerate growth.



On Slide 17, we highlight the potential which we see for the overall category growth and also the potential for online to take a larger share of that 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 18 and our current trading. The market trends for Harm Reduced Products remains favorable And we continue the transition of our business into mainly a nicotine pouch category. On top of that, the online channel continues to grow relevance within the category. In terms of inflationary pressure on inbound costs, we reiterate our previous guidance that inflationary pressure on our cost base remains limited.



Given the non cyclical characteristics of the category, we remain confident Any additional inflationary pressure can be passed on. Looking ahead, we continue to see solid performance in our nicotine pouch growth. The successful turnaround in Norway creates a solid platform for profitable growth in core markets. The strong momentum we have in our growth markets is sustained And we continue to gain share of the total market. Since the beginning of the year, we have launched a test pilot for vape Products in the U.



K. On our existing U. K. Storefronts. Initial feedback from the launch has been very positive and we are currently evaluating next steps.



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 2 releasing benefits of scale. Lastly, we are very well positioned for the current difficult economic environment for consumers With a strong balance sheet and a non cyclical product and a capital light business model, we are able to remain flexible and strengthen our market position. As I wrap up, I would like to guide you to slide 19. There is over 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 And we're over 10 times the size of our nearest competitor. We have a symbiotic relationship with our suppliers whereby in addition to being a partner of choice for new launches, we are also the largest provider of consumer insights. We continue to welcome proportionate regulation and we often benefit from it. Our unit economics continue to improve as we scale and this is already evident in our core markets and we have a highly engaged team with core competencies across both the nicotine industry and e commerce. I would like to remind everybody on some of the key takeaways from today's presentation, our nicotine pouch volume has grown by 41%.



Our revenue has grown by 21% At constant currency, we're 22% outright and our EBIT has grown by 29%. We are very proud of the results that we have for Q1 and I would like Take this opportunity to thank the team for an outstanding performance during the quarter. With that operator, I will pass over

Q&A



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



Thank you. A couple of questions from my end. Firstly, the strong sequential acceleration you've shown here in the growth markets. You've had growth rates there of 40% to 50% in recent quarters, now almost 70%. Can you say something about how much of this you believe it's related to the California ban.



Is that the main driver here behind accelerated growth or is there anything else? That's my first question.



Well, I think first of all, Nicholas, I guess there is a bit of an FX tailwind that we're benefiting from here, although we have benefited from it a little bit in prior quarters as well. What we are seeing is that we are showing generally very strong growth across the U. S. And if I take a look at California itself, I think it's probably worth noting that we had a disproportionately low share in California going into this environment. If we were to revert back to the early stages of 2022, both of our warehouses at that stage in the U.



S. Were hinged on the East Coast, hence, our convenience into California was a little bit, it had room for improvement at the time. Seeing this regulation coming in the latter part of 22, we chose to launch a West Coast warehouse work based on Colorado to be able to handle this dynamic going into California. So we were seeing an improvement in California prior to the ban. We have seen an uptick within that, but the vast majority of the uptick that we are seeing from that 50% to 70% in local currency terms, it's not coming from California.



I think California is accounting for maybe a high single digit element of that.



Super. That's very clear. Thank you so much. You mentioned in the report you talk about pressure on the product margin in Sweden due to campaigns in the start of the year. Is this something that was temporary?



Have you seen this easing gradually in the quarter?



We had, yes. So this was something which was in the same way as we ourselves had loaded some stock to have competitive advantage going into the quarter because of the excise increase, it was something which was which also had a little bit of an impact on the overall market dynamics during the quarter. So we did see a slightly more competitive first half of the quarter and we see it as a quarter which is going to return to normal from the middle of the quarter on.



Thank you. That's very helpful. You talk about vaping here in the U. K, and you say you've had a very satisfactory initial evidence here, and you're still evaluating. What are you evaluating?



Can you elaborate a little bit on what could be your potential next steps? I assume you mean investing more in the category. Do you also consider expanding to other markets?



Yes. So I think both. So this is our first time to move into a category which is not product sold in a can. And there was a we needed to launch this as a pilot in order to get the learnings as regards to where we needed to adapt different parts of our infrastructure and different parts of our model. I think we have the majority of the learnings got at this point in time, and we're quite happy with the progress that we've been making so far within the UK.



Now I think we're evaluating exactly how to adapt and tweak a few things in order to accelerate that Both within the UK, but also to prepare for expansion across other geographies also.



Very clear. Any news on what geographies could be relevant? Can you elaborate on that or is it too early?



I think we'll be back in further quarters with a little bit more detail on that space. Super clear.



Regulatory risks in Norway, can you tell us a little bit about Can you elaborate a little bit what you think would be the likely time line here for regulation? And obviously, being aware that Regulatory processes tend to take a very long time, but can you say something on what you think is the likely outcome here over the next few quarters or years?



Yes. Well, I think firstly, this needs to be taken into account as regards to the strategic paper, which has been Which is a process which generally relates to the next 4 years. It can occasionally extend a little bit further. And it's not unusual for these papers to come through. I believe this Can't you the 4th one?



I think we just come in this 4 year window at this stage. Not everything within this space tends to Coming to regulation, it's more of a bucket list of an extended sort of range of wishes coming through. There is quite a broad spectrum of dynamics within that strategy paper across multiple nicotine and tobacco categories, Including across the retail of them. Now we feel very confident that the piece around online It's been taking somewhat out of context and that digital in general is being bucketed together as opposed to digital marketing and online. We feel very confident that common sense will play out when it comes to an online ban here because Not only are we, as I kind of alluded to through the presentation, not only is online the channel which has gotten the strongest Age gating and age verification of any channel in Norway, but online is also A space with not only, prohibition of under-18s, but it's also a space With disproportionately low share of the 18 to 25 year old market, because in general, people with lower disposable income such Students or people which have just started their career tend not to go out and prepurchase their snus for the next month.



So we tend to have a disproportionately low share of under 20 Not to mention the solid age verification that we have for everybody, which is would attempt to buy, which would be under 18. So we feel very confident that The regulation that this strategy paper simply contains a bucket list of all and that it is highly unlikely to come in, in this space. And we also believe that many aspects within the overall strategy paper will Take many years to come in and may overrun into a the next parliamentary session We in Norway after an election.



Thanks for that answer. And Obviously, being very hypothetical here, but if you were to see an online ban in Norway, is there any I mean, what Do you have any clear plan B? Is there any option to your current setup? Is there any way you could continue to sell into Norway? Or would you have To cease operations in Norway entirely.



Again, this is a hypothetical question, but just curious what you're thinking.



It's extremely difficult to answer on the basis of we're dealing with effectively a paragraph Around this at this point in time in the strategy paper, so it's very, very difficult to determine what this could actually look like over the next 3 to 5 years. I think we would need more clarification before we would understand what potential impact it might have on the business.



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



Thank you, Nicholas. Thank you very much for taking the time to join in And look forward to updating you in 3 months' time regarding our Q2 performance. Have a wonderful day. Bye bye.