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Haypp Group AB (HAYPP.SE)

Q3 2024 Earnings Call

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MANAGEMENT DISCUSSION SECTION

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This call is being recorded. Your line is muted. Welcome to Haypp Group Q3 2024. 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 Key five on their telephone keypad. Now I will hand the conference over to the speakers CEO, Gavin O'Dowd and CFO Peter Deli. Please go ahead. Thank you. Good morning, everybody, and welcome to our Q3 2024 interim results. Our CFO, Peter Deli and I Gavin O'Dowd will walk you through our results. I would like to start by reiterating our higher purpose of inspiring, healthier enjoyment, joining millions. Moving along to the operational highlights. I would like to begin with our NPP Q3 volumes there with year on year growth of 42% and 93% across the two year periods. Nicotine pouches accounted for 63% of our total volumes for the quarter, up ten percentage points versus Q3 2023 as the robust trend continues. We are particularly happy with the continued strong volume performance in our growth division, which grew 58%. In addition, Nicotine pouches continued to show strong performance in the core markets, growing 32%. With that, I will hand over to Peter for more depth in our commercial performance, after which we can walk through other aspects of the business. Thank you, Gavin. Good morning, everyone. Let me start or financial overview with our sales development in Q3 2024. We grew sales by 25%, excluding the effects headwind. This means a further acceleration from our Q2 growth and brings the year to date average about 20%. From a slow start of the year, then we are looking at the contribution of the business units. We are ahead. We are very happy to see that both growth and core markets are significant contributing to the group growth, and also that the improvements in the emerging segment sales makes it a real contributor to our year over year sales performance in both segments. Nicotine pouches were the key driver for the growth. Out of the 25% growth excluding effects, it's accounted for the actions we put in place in order to manage the decline largely presorted. And this category drives largely remain flat versus last year. Moving to Slide seven and our profitability. Profitability also remained robust. This is consistent with the previous quarters of 2024. Our adjusted EBIT grew by 81% to 33.1 million PSEC, which means the 3.5% adjusted EBIT margin, an improvement from 2.4% last year. The result was supported by the sustained margin expansion, which we partly reinvested into the team, mainly to support or emerging segment and growth markets profitability before investments into the emerging segment reached 4.3% on an adjusted EBIT level. Important to highlight that in the quarter we created the reserve for the San Francisco complaint. Based on the available facts supported by external legal advice. Moving to the next slide to our forward markets. Here in core markets, we achieved a 16% growth excluding the effects headwind of 3% in Norway driven by the nicotine pouch category, which performed well in both markets. The nicotine pouch volume grew 32% and consistent performance both in Sweden and Norway. Profitability wise or adjusted EBITDA is up by 0.7 percentage point versus same period last year, driven by the improved media and insights revenues which demonstrated the robustness of our business model. Moving to Slide nine and growth markets. In all growth markets, our sales grew by 44%, excluding the 4% currency headwind. We are happy with the nicotine pouch development across the board in both markets. Adjusted EBITDA was 2.5 million, SEK 0.9% of sales in line with previous quarters. Active was exceptional. The increased search volume demonstrates the opportunity we see for for the further online channel penetration growth across the markets like that and or emerging markets. In the big scheme of things, these markets are still small. However, the sequential quarter over quarter growth remained robust versus Q2 2024 or sales is up by 64%. Active customers now reached 20,000 within the quarter. The investment for this business segment remained consistent, and EBITDA for this business unit was 7.8 million in Q3. This represents a 0.8% reinvestment on a total level. Moving to Slide 11 and or selected KPIs. Here, I would like to highlight two numbers. Firstly, the investment level, because year to date, Q3 invested 69 million SEK, which is 2.5%, slightly above the historical averages. But as we highlighted it several times earlier, this is not a flat line. Right now we are working hard in the overhaul of our back end and front end infrastructure, which is not visible in these numbers. However, as soon as these projects are completed in the coming quarters, this number will go down to the previously previous levels. For net debt to adjusted EBITDA ratio is 0.8. Looking at the last 12 months, which shows and represents the very robust and healthy balance sheet what we maintain for the group. With this, I hand the word back to Gavin to guide us through all the legal and regulatory developments. Thank you, Peter. Moving to Slide 12, covering some legal and regulatory areas, we are encouraged by Sweden's recent policy improvement as it moved from the lower nicotine consumption to the focus on bahco and nicotine harm, reflecting the benefits of risk reduction. In addition, the U.K. has recently reintroduced its tobacco and nicotine bill, reinforce seeing the

important the risk reducer products. I had two regulatory challenges in the latter part of Q3. In Sweden, Stockholm Municipality made to withdraw coldenrove snus. We firmly believe that the decision was unjust and we are repeating it through the court system. During the appeal process, we will continue to sell traditional snus as normal and we believe that the process will take 1 to 2 years to conclude. In the meantime, we have implemented all of the recommendations from the municipality and we expect a very limited impact on our sales. Secondly, the city of San Francisco's attorney has filed complaints against us and the Randoll online stores regarding the sale of flavored nicotine pouches into San Francisco. There are multiple locations in the U.S. where we restrict flavored products due to local legislation. However, we did not do so in San Francisco as we had received a or legal opinion from a credible law firm supporting our sales to the city. This opinion was issued in 20, reaffirmed earlier before the case is ongoing as we speak. In addition, California is introducing new legislation which will remove the exemption for online retailers who sell flavored and nicotine sorry to sell flavored nicotine and tobacco products into the state. Moving to Slide 13. The upcoming legislation in California, which extends the restrictions on flavored products to include online, has meant that we have suspended sales, most of which was flavored products into the state until we have further clarification. While California represented circa 10% of our nicotine pouch volume in Q3, the growth levels were substantially lower than the rest of the country. This new legislation impacts not only flavored nicotine pouches sold into the state, but also oral tobacco. Oral tobacco products such as msti and snus. We are already a rapidly declining share of our U.S. sales and circa half of them were being sold in California. As a result, the group has brought the exposure to tobacco from 25 to late 2024 through to slide. The US continues to represent an ever increasing peer group percent of the group volume during Q3. I would like to take this opportunity to provide more depth and breakdown of our U.S. business drivers of growth in the prior period. While nation France as stated in the prior slide while nationwide tobacco products and California's nicotine pouches make up circa 3% of the group volume, they effectively have not been growing. In addition, from the latter part of Q3, we have experienced a challenge in sourcing. If the outlook for our ZYN sales in the US that the order offer quality products to our consumer reach versus our individual brands as highlighted in our Q2 release, other brands which have been on the market for some years, start to show robust share growth from late 2023. This is driven by increasing consumer awareness and brand equity. These brands are effectively the drivers of all of our U.S. growth. In addition, new brands from large international manufacturers have and are expected to come to the market during 2024. These are further broadening the range of quality nicotine pouches for our customers. Now to take a look at our long term performance, on our outlook on the next slide. We recognize that is just over three years since we have listed on the stock market. I would like to take this opportunity to look back on our sustained and business performance over that time. Starting with strategically important nicotine pouch volume, we have grown over 250% since early 2021, bringing it from 31% of our volume to 63% of our volume in Q3. In addition, we have also entered the vaping category, which now accounts for just over 2% of our volumes. Also during this time, we have increased our EBIT margin. The group intends to provide a set of longer term targets to the investor community in the spring of 2025. Moving to Slide 17. In addition to the strong set of results in Q3, we would like to reiterate the robust fundamentals for risk produced products, the suitability of online for the category for a variety of reasons, not least of which is the traceability and control and strengthening position within the online channel. The rapid and sustained growth of nicotine pouches is expected to generate increased scrutiny, and in many cases this scrutiny is warranted. We will continue to invest significantly into compliance, and we recognize that it is not only a source of sustained, competitive advantage, but it is also the right thing to do. Moving to our final slide, we would like to reflect on the dynamics underpinning our continued performance. Hype has a substantial component, and in its model we can turn robust systems for growth is the result of an excellent team team. Therefore, the connection to our purpose of inspiring women for millions. I would like to take this opportunity to thank them for their commitment, dedication and overall performance. With that, I will hand over to the operator for questions. If you wish to ask a question, please dial pound qis5 on your telephone keypad to enter the queue if you wish to withdraw your question, please dial pound key six on your telephone keypad. The next question comes from Nicholas Ekman from Carnegie. Please go ahead. Hello. Good morning. First question here on the withdrawn Swedish license, do you have any further news here and the dialogue with the authorities on this issue ? And I guess, as a first question, have you already submitted your appeal and do you have any indication if the changes that you've already made, if those could be sufficient for for this license

to be given back or just any any of your thoughts here on the process would be appreciated. Thanks. Good morning, Nicholas. And yes, we have submitted our appeal and that moves the process into the legal system. So it's no longer to the same extent in dialogue with the municipality. It has now moved into the parallel infrastructure here or the legal system as it goes through. And as I said, we have over the over the last six weeks, we have implemented all of the recommendations which the municipality raised, some of which were only implemented as recently as last week. And so they're all now completed at this point in time. However, I don't expect that the position from the municipality is going to alter at this point in time. I think this process is going to be brought through the court system where we expect that we will get the right conclusion coming through there. Very clear. Thank you. And just to clarify, you had 11 million of one off costs here. I didn't really understand. Was that related to legal fees or is that a provision for the fines that you're expected to receive in San Francisco ? Good morning, E-club. Basically, that covers the expected settlement fee with the with the city. And also the city's legal cost is included in this reserve. But this is based on the very initial estimations because we are still in the data gathering fact for the case. Okay. Do you do you see any risk that that fee could be significantly higher, meaning like 50 to 100 million ? Or do you think 11 million is is not the absolute best estimate ? I think it's probably fair to say, Nicklas, that that's our best estimate at this point in time. That's fair enough. And any reflection on the change of administration in the U.S. ? I think in the past, Republicans have generally been more relaxed on regulation. Do you think or do you have any indications about how the regulatory environment in the U.S. could change, and if that could be to your advantage ? I think it's still a little bit fresh at this point in time, not just because of a Republican administration within the White House, but also with the impacts of having control on both Congress and the Senate. And your hypothesis is correct. Historically, the Republican administrations have been more supportive of an have been more supportive of our category in general. And there has been some statements coming from the White House regarding this or from the incoming administration regarding and risk reduced products in general. However, I think it's a little premature to determine exactly what the specifics of that will be. So I think we would like to keep a close eye on how this evolves and perhaps have a little bit more guidance once they we get to the Q1 results provided the administration should have been draft policies a bit clearer on many of these aspects. Absolutely. Fair point. Also, just wondering about your margin development now. It's risen very consistently at around 110 basis points in the last three quarters. Looking at the year over year effect and what do you think is the likelihood of another 110 basis points going into next year ? And obviously, there's a lot of uncertainty here. But do you think that the the scale benefits, the improved negotiations with suppliers, etc., do you think that that could be sufficient for a similar margin progression going into 25 ? Yeah. So I think what we have seen in recent years has been a material uptick as we move from one calendar year into the following calendar year where we we see many of the benefits of scale coming through in steps rather than coming through gradually throughout the year. And I think you guys are only recently familiar with this from prior years, and there's no fundamental reason for that to stop on the basis that as the group continues to grow, those benefits of scale, continue to give guidance at this stage as to what our margins will be for 2025. As you say, there is moving factors, but in addition to that, there is also considerations as regards to how much do we reinvest in different spaces as the opportunity ahead of us seems even greater than perhaps we previously expected across many markets. So I think it's probably a little bit premature at this point in time, Nicholas, to provide an awful lot of guidance for 2025. But I can confirm that what you were saying there as regards to the benefits of scale, which have been released in previous conversions from one calendar year into the next, would be expected to occur for next year as well. Okay. Very clear. Thank you so much. Those are all my questions. Thanks for answering. Thank you, Nicholas. Thank you. As a reminder, if you wish to ask a question, please dial a pound key five on your telephone keypad. There are no more questions at this time. So I hand the conference back to the speakers for any closing comments. Thank you all very much for your time. Greatly appreciate it. And I look forward to giving you another update in February. Thank you, everyone.

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