Verallia Q3 2020 Results

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Financial Highlights and Key Initiatives

Michel Giannuzzi

CEO, Verallia

Welcome

Thank you very much. Good evening, everyone. And thank you very much for attending this call meeting about the nine-month results of Verallia Group. I would be very pleased to share my presentation with Didier Fontaine, the current Group CFO. And please be aware that also Nathalie Delbreuve, who will be succeeding to Didier as the Chief Financial Officer as of 2nd November next week, will also be attending the meeting. So we are very pleased that both of them are able to participate to this meeting.

And without any further ado, I will start my presentation with the first slide, which is financial highlights of the quarter and of the nine months.

Q3 Volumes Better Than Anticipated

But please, I would like first of all to draw your attention to the Verallia profile on the left part of the slide to explain a little more in details why this profile has enabled us to be so resilient during the year 2020, which has been a challenging year for every industry indeed.

And the first thing I would like to highlight is the fact that as you can see on the doughnut, we have very diversified and balanced end-market exposure, which has been very useful to especially grasp the growth in some segments of the market that have been growing extremely fast during the lockdown or during the recession, especially in the second quarter and even after that, and I mean by this, the food glass packaging.

And also, if you see below the fact that we are leaders in Europe, of course, has an implication, the fact that we are not only exposed to the premium segment, where as you know very well as you recall from the IPO presentations, we are quite strong in this premium segment, but you cannot be a leader in Europe with only premium products. Which means that of course indeed we are also competing in all other segments of the market including the entry or mid-mass market segments, which of course have been probably more resilient during this year than the premium market that has suffered a bit more.

And the last thing I would like to say is that the combination of those diversified end-market segments and the many countries we are present in; the 11 additional countries where we are present, is giving us the opportunity to balance and follow the market trends that can be different from one market to the other with kind of much more resilient factors than maybe pure players in one country or one segment of the market. Let me give you a concrete example. According to national statistics in Italy, you know Italy is the largest wine producer in the world and the wine, still wine especially, is our largest segment. If you consider the Italian statistics, the winemakers in Italy have been exporting in the first half of this year 3% less in volume in hectolitres and 4% less in value compared to the previous year. Whilst at the same time, the French wine producers have seen their exports going down by 10% in volume and 21% in value during the first half of the year.

In other words, the French wine producers that are exporting have lost market share at export against the Italians knowing that for the top 11 exporting countries in the world, the drop of volume has been 6% for the first half of the year. So Italy has been gaining share. One of the countries where Italy is gaining share to export is indeed United States, where you know that the Italian wine producers were exempted from the US tax that were imposed a year ago, which was not the case of the French wine producers and the Spanish wine producers, the two other largest wine exporters in the world.

So this exposure that Verallia has in the three biggest wine exporter markets in the world, France, Italy and Spain, and the fact that some markets are gaining share to export service has enabled Verallia to take advantage of this diversification that I was mentioning before. The second thing that I would like to draw your attention to when you look at this split of end-markets and the fact that food is a quite important segment for Verallia is that even though we estimated during the first semester that about one-third of our customers sales are made on-trade, which means on the hotels, cafés and restaurants, we have seen during the confinements that some shift from on-trade to off-trade. Some volumes were shifted from on-trade to off-trade. And jars is a very good example of that shift that we are seeing, and this also is an explanation for I think the strong performance of the company in the first nine months.

Last but not least, I mentioned the fact that we were strong in the premium segment. But if you recall what I said during the presentation a year ago, the fact that we are quite strong in this premium segment is not so much the evidence of the capacity we have to make very nice products, very customised products for our customers, but more the fact that we have equipment, facilities, plants that are flexible enough to make short production runs because you know very well that in the premium segments, you do not have such long runs as in the mass market segments. And we have taken advantage of our capacity to change over our operational lines fast to adapt to the new customer demand trends to, of course, grasp any opportunity to grow our business during this year. This flexibility has been evidenced, for example, by our capacity to shift very quickly some lines of production that were producing bottles into lines of products that are now producing jars, for example, to follow the strong demand in jar and also this productivity is being used every day as we speak to follow very unpredictable customer demand.

I mean, let us be honest, our customers' forecasts right now are very hard and very difficult to follow because they are very volatile, and the fact that we have this flexibility has probably given us some kind of advantage too that we can use to explain the very strong performance of the first nine months. So this introduction being done and this is evident by the left-hand part of the slide let's look at a few numbers now.

9M 2020 Financial Highlights

First of all, we are very pleased to report that over nine months the reported sales are only 1% down versus the first nine months of last year. And more importantly, the organic growth for the first nine months is up 2.3%. And even if you exclude Argentina, that is a boost to our organic growth, as you know, it is still a very nice 0.9% organic growth for the first nine months year-on-year.

And this has been extremely boosted by the third quarter, where we reported a 5.3% revenue growth and an 8.9% organic growth during the third quarter. This strong performance on the top line has enabled us to maintain an adjusted EBITDA at almost the same level of last year at €474 million for the first nine months. Last year I remind you we were at €478 million and with a slight improvement of EBITDA margin by ten basis points up to 24.3% of net revenue.

You know very well that we are very focused on managing also the balance sheet very tightly and very carefully, and we have continued to deleverage the company. We are bringing the ratio of net debt to last 12-month adjusted EBITDA from 2.7 times a year ago to 2.2 times at the end of September of this year.

And those very strong results of this first nine months of the year have encouraged us to revise our guidance for the year, including the latest news that has been made in the last 24 hours in France and in other countries regarding the more severe measures taken against COVID. We have the confidence to upgrade our guidance to the numbers that I will provide to you in a few minutes. So this was the first highlight for the quarter.

Verallia Purpose

If you move to the next page, you will read here that we have also worked in the last nine months together with 1,500 employees, customers, suppliers, investors and also other local community members. We have worked together to define the Verallia purpose, which we were very pleased to announce a week ago. Our purpose is to re-imagine glass for a sustainable future.

Clearly, this purpose is already fully integrated in our strategy, is leveraging our company values that are almost 200 years old and clearly with a strong and clear focus on to circular economy that we want to promote and of course improving the carbon emissions to avoid the global warming or to maintain the temperature increase well below two degrees. So this is something that we announced a week ago. We'll be in the coming weeks communicating a lot more about the concrete measures and objectives that we are taking in this respect, but we are very proud to communicate to you that we have made this very important work during the first time also this year and we are pleased to report that to you today.

Two New Innovative Product Launches

Moving into more recent news regarding innovation and product launches. You have here two interesting examples of a co-design innovation, especially in the perspective of leveraging reuse concept, which you know very well about the recycle concept, the fact that the glass is definitely recyclable, but we also work on reuse. And here you have two examples of reuse bottles that have been developed by Verallia recently.

The first one is the Gobi Indoor water bottle, which Gobi has sourced 100% in France and through lifecycle analysis has been able to demonstrate by using this water bottle during three months that will compensate the carbon emissions that PET bottles and plastic cups are generating during the same period.

On the right-hand side, it is another innovation which is the SodaStream that I am sure you know very well. The SodaStream machine today is either dedicated to glass or to PET. And SodaStream has developed a new machine that can be versatile, can be used either with a glass container or PET container and we are very proud that we have co-developed this nice glass bottle that will be able to resist to carbonated liquid and of course in a reusable way, in other words, you can put it in your dishwashing machine and it will of course remain as efficient as on the first day.

So with those two of product innovations that are interesting because it shows that we are not only focusing on recycling. We spoke a lot about recycling in fact, but we are also trying to contribute on some reuse solutions that are of course very good for the environment, and we are pleased to report that to you.

Augmented Intelligence Deployment at Verallia

Now moving to the next page, we are also pleased to give you some evidence into the interesting work that we have done on the R&D side, developing augmented intelligence. I prefer this word rather than artificial intelligence. And data has been recognised with an Enterprise Trophy given by RH&M Group.

And Verallia was prized, if you want, for in a very traditional industry like the glass-making industry being able to use those innovative solutions either for example to control our furnaces and to improve the efficiencies of our furnaces either to improve the implementation at the end of line inspection in the quality machines that we have or to also improve the process control on the foaming machines that we have in our factory.

These were three examples where we used augmented intelligence at Verallia, and again not only we will work on the innovative designs and products, but we will also work on strong innovation especially on the process side. And more will come, I am sure in the next quarters.

So this being said, now I will hand over to Didier, who will you go with you through the financial results.

Financial Results

Didier Fontaine

CFO, Verallia

Agenda

Thank you, Michel, and thank you very much for all of you to joining this call. As usual, I will cover the financial matters in three parts. Firstly, we will start by reviewing the revenue numbers at Group level. I will then move on to profitability with the review of the adjusted EBITDA and then we conclude on our cash performance and our updated capital structure.

Better Than Anticipated Volumes in Q3

So let us move to page nine. I have insisted here at the beginning of the call volumes in third quarter has been better than expected. Actually, volumes have been growing by 4.2% versus the third quarter last year, leading to a strong 8.9% organic growth. As you remember all, volumes were down 7.9% in Q2, and during our H1 review in July, we were indicating that June numbers were much better than the April ones and the trend has continued in Q3.

As a consequence of that, the sales posted a very solid 8.9% organic growth in Q3 versus a minus 5.4% in Q2. Just two seconds over that sales number, then we would like to come back to what Michel said in introduction about our portfolio diversification. The minus 5.4% indeed is a negative number, but even though it was negative, it was probably the best number among our peers in Europe in Q2. Therefore, showing the benefit of our product portfolio and the original span as well.

So over the first nine months, the Group achieved a revenue of €1,956 million to be compared to €1,976 million in the first nine months of 2019. This corresponds to a slight 1% decrease in reported figures, however, almost recovering from the tough Q2. On an organic basis, if we exclude the conversion impact, revenue grew by 2.3%, all in, and 0.9% if you exclude Argentina.

If we go by geography, the volumes improvement over Q3 is basically mostly due, on the one hand, to the very swift recovery and the very dynamic environment in Latin America, especially in Brazil, where despite a difficult political and sanitary context, the market is pulling a lot today. We mention Italy. Italy has been posting very strong volumes increase, mainly due for a the good part to our customers' exports. While in Iberia, volumes have been picking up nicely as well.

If we move from geography to product family, we mentioned non-alcoholic beverages, and especially food jars. Food jars had been the product category that has done extremely well during the crisis, and I think very well oriented, and we believe this is the trend. And the still wine, where our inventory is higher in terms of tonnes sold compared to last year, especially come up from Italy and from Spain.

In addition, in the third quarter, our top line enjoyed a positive mix and continued to benefit from the contribution of the price increases that have been carried out at the start of the year.

And lastly, I will say, as usual, and most unfortunately, we are still have been penalised by the exchange rate variation, which has been high given the current economic turmoils. The impact was strongly negative reaching 3.3% of sales over the nine first months, representing an overall rate of €66 million, driven mostly by the currency depreciation in Latin America and especially in Brazil. If you look at Brazil between the closing rate of September 2019 and the closing rate of September 2020, the real lost 45%. And given that Brazilian real represents almost 50% of that negative hit.

Adjusted EBITDA Back to Last Year's Level Despite COVID-19 and Forex

Now we have covered revenue, let us move onto the adjusted EBITDA on slide 10. Adjusted EBITDA of the first nine months is back to last year's level, which is, I think, a very good and solid news despite the heavy negative impact from the COVID-19 and the forex transactional impact, reaching €474 million. Organically, if we remove the forex, it increased by 3.9% despite all what we had since the beginning of the year.

This performance I am going to repeat it again, but I think it is always good to repeat the simple stuff. This performance has been driven by the rolling out of our three pillars. And if you allow me, I will highlight some key points of the three pillars that happened in the third quarter, so that it will help you better understand the bridge year-to-date.

Activity remained negative over the nine months and has been negative in Q3. However, in Q3, we benefitted from a positive operational leverage, that partly offset the anticipated negative impacts of the destocking resulting mainly from our planed and extended furnace repairs. We reduced the level of inventories between the end of June and the end of September by almost 10%.

Our second pillar that was again very solid in Q3 is supported by the improvement of both the product mix is our positive price mix cost spread. Very good performance in Q3 contributing and reinforcing a good price mix spread over the nine months.

Finally, the third pillar, i.e., our capability to reduce our cost base by our productivity actions. This third pillar has continued to deliver. Keep in mind; we have a 2% reduction target net cost cash base, production cash cost base. The performance action plan led to a net reduction in cash production cost for the nine months, representing 2.3% of production cash cost, i.e., €28 million.

To complete the picture, the Other column includes mainly the COVID-19 direct extra costs for €4 million. By the way, the total cost for the year or year-to-date COVID has been €14 million for the company so far, €10 million is recorded in adjusted EBITDA. The €4 million Other that are partially PPE and donations are recorded below the line. And out of this €10 million booked in adjusted EBITDA, majority of that is into underactivity and is recorded under the pillar activity, a negative impact in activity and the rest is booked in the Other column.

As a conclusion, in spite of those headwinds, Verallia has been posting a very solid EBITDA margin at 24.3% over the first nine months of the year, which is higher as Michel was saying eight basis points, but higher than the 24.2% over the first nine months 2019, proving once again the resilience of our business model.

Cash Performance

Now in order to cover revenue and profitability, let us look at reality, which is cash. I review our cash flow performance, improvement in our leverage and our capital structure. Let us move to slide 12.

Continuous Deleveraging Capabilities

Our debt reached €1,359 million at the end of September versus €1,627 million one year ago. This net debt represents 2.2 times adjusted EBITDA for the last 12 months. It was by the way €1,591 million at the end of 2019, which represents a reduction of almost 15%, i.e., €230 million reduction in value over the first nine months of the year.

All that put together, those numbers compare very favourably to the past. 2.7 times leverage at the end of September 2019. 2.5 times leverage at the end of June 2020. This is confirming again our capability to reduce leverage from 0.4 to half a turn per year after dividend. And this is confirming the capabilities of this company as well to generate a very robust free cash flow to equity via not only the results but the control and the mastering of the balance sheet is working cap and via its discipline as smart investment policy.

And just for the sake of clarification in case some of you have some doubt, the leverage ratio remains well below the maximum leverage ratio set out in our financial loan documentation, which is at five times adjusted EBITDA. Clearly, you understand that is not something that should keep us awake at night.

Verallia’s Net Debt: €1,358 Million at September 30, 2020

Now if you are moving to slide 13, and as mentioned at the beginning of this presentation, Verallia has a strong balance sheet that underpins resilience in these critical times. By the way between June and September, nothing much the structure per se has changed, a simple fact that on 30th September, we have fully repaid from our cash balance of €200 million RCF drawn mainly mid-H1 since the commercial paper has been reopening up.

Therefore, we use our cash to repay our loan balance.

Interesting to note as well, as I was saying, the reopening of the commercial papers market. We remain very cautious. We have seen the crisis that being a BB- market can close very quickly. We have been able to draw and find another €120 million. We have not pushed. We could have done much bigger, but today we are much more focusing on pricing and duration with the capability to go up to 12 months.

In addition to the good cash performance, the decrease of the leverage below 2.5 times last 12 months adjusted EBITDA as of 30th June allows us to lower by 20 bps our TLA and RCF1 margin. The change in the margin is effective as of 3rd August 2020, and this is going to represent the yearly saving for the company of €4 million cash in financial charges.

I think you will join me to say that the liquidity remains very solid. Actually, at the end of June, I was frustrated that we were shy of the €900 million by €3 million. We reached €897 million. This time we beat the €1 billion liquidity at the end of September, which speaks by itself and should continue to build up.

Well on my side, this is it. That was my last financial presentation as the CFO of Verallia, the company I have been very honoured to work for over the past few years. My last word is to say that I am leaving a Group with solid fundamental prospects and a solid and very dedicated financial team starting with Nathalie, to whom I am handing over with confidence after this call.

Thank you all for having listened. And now I give the floor back to Michel.

Conclusion and Outlook

Michel Giannuzzi

CEO, Verallia

Conclusion: Solid Q3 After a Resilient H1

Thank you, Didier, and stay online for the questions. So it is time maybe to conclude and to wrap up this presentation. First of all, as you understood from this call, we have had a very solid Q3 after a very resilient H1.

The volume increase in Q3 has led us to report 8.9% organic growth in Q3, after a 5.4% organic decline in Q2 and a 4% increase in Q1. So quite a very nice recovery in the third quarter. And to be frank with you, quite unexpected as well.

So that puts the first nine months of the year at 2.3% organic growth at the end of September. The adjusted EBITDA margin has been maintained more at the same level, with a 24.3% margin over the first nine months. And we have kept deleveraging this company half a turn year-on-year, and at the end of September, we are pleased to report the leverage of 2.2 times last 12 months adjusted EBITDA after the €13 million of cash out for the dividend payments.

2020 Guidance Upgrade

So based on these very strong results of the third quarter and including taking into account the latest developments and announcements related to COVID-19, of course, providing that the pandemic does not significantly deteriorate further by the end of the year, we are pleased to upgrade our guidance for 2020.

The volume for the year should be slightly below 2019. I remind you we said in July to be around minus 5%. Here, which would be a low single-digit down in the year 2020 compared to 2019. We expect a slightly positive organic growth for the full year. We revised upward our adjusted EBITDA guidance, which will be now around €590 million. If you remember, we mentioned €543 at the end of July. So it is quite a significant I would say improvement in the EBITDA guidance.

We will keep generating cash in Q4. Therefore, the cash flow will be very strong and solid in order to maintain the leverage between 2.2 times and 2.3 times last 12 months EBITDA.

Mid-Term Guidance as Confirmed in July 2020

And of course, indeed we confirm and repeat the mid-term guidance that we mentioned in July on all of the mid-term objectives excluding the organic sales growth, which we will be probably waiting for the kind of economic and COVID-19 stabilisation to give you a better guidance on the mid-term organic growth.

But you understood from these first nine months that we are a company that is eager to keep growing in a profitable manner, improving both the top line and the bottom line at the same time.

So that was it for our presentation tonight. And we are very pleased now to answer your questions.

Questions and Answers

Matthias Pfeifenberger (Deutsche Bank): Yes, good evening ladies and gents. I hope you are all well and safe. Thanks for taking my questions and congrats to these very strong results. The first one is clearly on the second wave. Can you share some thinking on that? Actually, did you have a higher fiscal EBITDA target maybe a week ago and just trimmed it a bit because of what is happening in the last week? And also you said the guidance is under the condition that it is not deteriorating significantly, but that is what is happening in the market. So the question is how safe are you with regards to this implied minus 15%, 16% on EBITDA? Thanks.

Michel Giannuzzi: Thank you, Matthias, for your question. Indeed, we have been monitoring the global situation on a daily basis almost hour by hour for the last 24 hours. And this guidance is the latest revision, if you want, that we have made available today. This includes everything we know so far, which basically summarises or sums up to more drastic measures in the lockdown of hotels, cafés and restaurants in many countries, starting by France, Iberia, Italy, maybe Germany.

But as you have seen in Q2, we have seen that even when there was significant – actually Q2 it was almost a full closure for two months of hotels, cafés and restaurant. So there has been some slight offset or slight compensation made in the retail chain. And therefore, the impact remember for Q2 for Verallia was not the mathematical calculation if you take into account that around 30% of our customers' sales are made in the hotels, cafés and restaurants.

In Q2, our volume dropped single-digit, high single-digit though, but still single-digit in volume. And therefore, we do not expect, of course, to see such a sharp drop in Q4.

The second thing is Q4 is a small quarter. I remind you this is, I would say, the lowest quarter of the year for us. And therefore, again, that we have factored into our forecast the fact that Q4 will be quite less impacted, if you want, if anything happens, than the other quarters.

And the third thing that you need to have in mind that makes us confident about our guidance is the fact that because we have been surprised by the strong sales in Q3, we have ended up the quarter with a very low level of inventory; actually to be honest with you, too low level to satisfy our customers' needs. And therefore if anything, if the sales are softening in Q4 more than what we expect, it would be an opportunity for us to rebalance our inventory and rebuild some inventory to better serve our customers.

Matthias Pfeifenberger: Okay. Great. I have got a question maybe you want to comment on the valuation discount to some of your peers. I mean, you had the best performance in the second quarter. Now, these set of results continue their track record, but still, you are on a substantial discount. And related to this, can you share some light on your UK exposure, although with respect to some of your peers? You are probably not among the market leaders there.

Michel Giannuzzi: No. As you know, we have no operations in the UK. The UK is not one of the countries where Verallia is present. Having said that, some of our customers are exporting to the UK. For example, we know very well that some of our wine customers in Italy are strong exporters to the UK. We also have some customers that are buying directly from French brands, some bottles. But it is a very marginal business for us. So we are not so much, I would say, concerned about what can go on with Brexit.

Matthias Pfeifenberger: And the last two are basically housekeeping. I mean, is it fair to say that if we exclude the price increases from Argentina, the price cost spread is quite narrow and obviously that is not needed because we do not have a lot of cost inflation, I guess. And then also did you see some ramp-up effects from the new furnaces already in the third quarter or what do you expect in the fourth quarter? Thanks a lot.

Didier Fontaine: I will take that point. Good afternoon, Matthias. If we exclude Argentina, the price remains reasonable because do not forget Argentina is not a major country for us. The big number reaches a low level. Globally, the price increases have been correct everywhere, all across the board, all across the Verallia companies. And relating to the new furnaces, I think in Brazil notably Jacutinga have done an extremely good job, is fully loaded. And that is the reason why we think the market was pulling a lot.

Alexander Berglund (Bank of America): Thank you very much. Good evening. Well, first of all, congratulations on a good result in these uncertain times. We have a follow-up on what Matthias was talking about on kind of visibility, etc. here. And I think it has been a question from the investor base as well because there have been surprises for Verallia. I mean, positive ones.

So do you feel that your sense of kind of what happens for the business in this environment has increased? That your kind of predictability has increased? And more specifically also in your conversations with your customers, do you have a sense that your customers have a better understanding what end demand, etc., will be or could be in different scenarios? So that is my first question.

And then secondly, if you can comment anything on supply and supply discipline in the market generally. We have continued to see quite good supply discipline. Thanks.

Michel Giannuzzi: Thank you, Alexander, for your questions. Regarding the visibility and the ability of our customers to read the market outlook, frankly speaking, it is extremely volatile. I would have told you maybe two months ago that we were on a recovering path regarding visibility and regarding the forecastability of our customers. But the last few weeks have shown the opposite actually. It seems that our customers have a very difficult time to figure out what they are going to say and when and where.

And that is creating to all the suppliers a huge challenge to be able to meet very volatile demand. And in this environment that is what I was mentioning before, our flexibility that we have built over years in this company has enabled us to react probably much better than some of our competitors to be able to follow what our customers were asking. But I am not confident at all that the visibility is improving in the coming weeks. I think we will have to live and to learn to live with a lot of uncertainty going forward at least probably until the beginning of next year.

So regarding your second question on the supply discipline. Clearly, I think as we mentioned a year ago during the roadshows of the IPO, I think we see an industry where everybody is, I would say, rational in the way that if the market is down, I mean, you need to adjust your own capacity to lower level of demand if you want to maintain your business in good shape. And this is what we have done. Of course, during the second quarter, it has been quite extreme because the slowdown has been very, I would say, important.

But even after the second quarter, we have seen some projects of new furnaces constructions being delayed. We ourselves have decided not to rebuild one furnace in France because the French market is not has done as the other market, and therefore it is even slightly down. And therefore we decided not to reconstruct one furnace in our plant in Cognac in order to, I would say, eliminate some unused and unnecessary capacity from the market. And this is what we have seen so far.

Lars Kjellberg (Credit Suisse): Just coming back a bit to your discussion going into the second half about obviously pushing all of your furnace repairs into the second half. I think you mentioned five that were going to go down for rebuilds in H2. So the question is how many have you now done?

The other question, I guess, relates to working capital because to your point you reduced inventory by 10% from a relatively elevated level after the second quarter. I understand that depends of course on strong demand as soon if you will find an opportunity to rebuild or not. But in terms of your production, how do you see that fairing? First and foremost, how did it fair in Q3 year-on-year, and how do you expect that to fair in Q4 on a year-on-year basis based on your plan?

And also finally, if you just confirm what sort of CapEx levels you are looking for in the current year and how we should think about that in 2021?

Didier Fontaine: Okay. So I will leave 2021 to Michel because I do not think I should comment on that. I will take the first one. What we have said. We have said that we are planning to do several furnace rebuilts in the year 2020, one of them has been performed in Q1 2020. We have done, I will say, two and a half because you do not close on 30th September. So we have done more than half in Q3. And as expected, on time, we have decided you remember well to extend a little bit as well.

Now from a working cap management, you know our working cap, you are right, the inventories have been a big contributor. It was a contributor last year as well, we are talking about variances of variances. Last year the inventories had been reduced between January and September the same year more clearly, we are 100k tonnes below at the end of September 10% than we were last year, September 2019.

However, overdues are fully in control. I mean, in terms of percentage of sales this is lower, despite the fact and we are improving our working capital without having recourse to more non-recourse factoring. We have 4% less non-recourse factoring than last year. So I think the balance sheet is pretty well under control.

Regarding the production, I think exactly what Michel has been saying; we have flexibility. We have flexibility if the market is not there to increase a little bit, selectively the level of production. And unless the level of absenteeism is extremely high, there is no reason why we shall not be able to do so. So we have the flexibility of production tool to address that if the sales are not aligned.

As regard to CapEx, I will mention cash because you know we have completed the two brownfields. In term of cash, we are going to spend around €245 million cash, which is sitting in more in cash than last year. So that was expected. If you remember well, what we said when we started the year, we said, okay, listen, the bulk of the CapEx is due in the middle of the year. So the payment terms make payables during the year. So we were going to have probably facially in value the same book CapEx, but with a negative impact on the payables, that is exactly what happened.

I leave it to Michel for 2021, but I do not think there are any surprises given our discipline and our requirement.

Michel Giannuzzi: So for 2021 Lars, our goal and target has not changed. It is the mid-term guidance that we gave you and reinforced in July, which is that we are going to spend 8% of our turnover in recurring CapEx. So our turnover being around €2.5 billion, it is around €200 million plus or minus a few millions that we are going to spend every year on the recurring CapEx.

Lars Kjellberg: And in terms of specific CapEx for next year, is there anything planned for next year because some projects were pushed, I suppose, maybe into 2021 or what does that imply?

Michel Giannuzzi: Well, we did not announce any adverse strategy CapEx in the past. The two that have been completed this year, which is the brownfield in Villa Poma in Italy and the brownfield in Azuqueca in Spain. Those two brownfields strategic CapEx will be started before mid-year next year, so the first half of the year next year. And that is it for the time being.

Now should any opportunity either from an M&A or from another reason be found, of course, we will communicate in due time about those strategic CapEx. But for the time being, that is what we have.

Didier Fontaine: And the cash on those brownfield has been largely spent year-to-date.

Lars Kjellberg: Right. Just in total, then you are looking at a CapEx cash spend you said €245 million?

Didier Fontaine: This year more or less. For 2020 that is the target we are having for the year, yes.

Lars Kjellberg: Very good. And just finally, there is some misunderstanding from my side. Your inventories are of course tight as you mentioned, but in theory then to reach your €590 million number that you are talking about or embedded in that guidance, is that production in line broadly speaking with shipments or do you have any meaningful deviation between the two?

Didier Fontaine: No, this is no meaningful deviation. This should be in line.

Michel Giannuzzi: Just to be very precise on this question, we are not planning to increase inventory significantly differently than last year. Q4 is always a quarter at the end of the year because it is a low quarter in terms of sales, but our factories are running 365 days a year and 24 hours a day. So the production output from factory is very constant throughout the year, but December is a low sales month. Therefore, every year we increase a little bit inventory in December, but we are not planning to increase it much differently than the previous year.

Lars Kjellberg: If I may just put in one more question. I think, of course, when you spoke in July, you talk about extended downtime and then what to expect and what is relatively subdued demand. I would assume that the extended downtime did not happen this year. If you can confirm that and how should we think?

Michel Giannuzzi: No, absolutely. I mean, of course, we were planning some extended downtime, especially linked to the furnace repairs, which of course we have not done because we were short of inventory.

Lars Kjellberg: Great. And furnace rebuild activity next year, is that going to be broadly the same as this year? Six, seven furnaces coming down?

Michel Giannuzzi: Yeah. Absolutely. So we have a more or less regular flow of furnaces rebuilt every year, six, seven furnaces a year.

Lars Kjellberg: Well done again, Didier in the quarter.

Didier Fontaine: Thank you, Lars.

Francisco Ruiz (Exane BNP Paribas): Hi, good afternoon. Congratulations for the figures and good luck to Didier in his new challenge. I have four questions, if I may? First one is if you could give us some light on the current price negotiation for next year?

The second question is, if you could give us what is the current situation of hedging both in raw material and energy and you could give us what is the delta versus the cost on 2020?

The third question is if you could give an update on the restructuring in France. And the fourth one, it is what is the current situation of the new furnaces in Villa Poma and in Azuqueca? Are they opening? Are they running at full capacity? What is the current situation? Thank you.

Michel Giannuzzi: Okay. Thank you, Francisco. I will take the first question. I will let Didier answer the second one, and I will take the following questions number three and four. So regarding the price negotiation, of course, we start the price negotiation soon, as you know in Europe. In Latin America, it is everyday price negotiations or almost in Argentina for example, but it is much more dynamic. But in Europe, as you know, most of our customers negotiate between October and February.

A few customers have a different fiscal year. They negotiate mid-year, but most of the negotiations are currently happening right now. So without going too much into details which of course for confidentiality reasons I will not be able to give you, the price negotiations, in many countries, are led by the inflation of cost factors. This inflation, especially on the energy side, can be different from one country to the others. Therefore, we do not have a general price increase in all countries, which is the same, as you know very well. So it is very much tailored to each country.

Now more than 80% of our negotiations are, I would say, annual negotiations and we have less than 20% of our negotiations which are linked to long-term agreements, where most of the case is the price formula. So when we have a price formula, the price formula shows that in some countries the pricing will be neutral or slightly down depending on the energy mix and energy cost of the country. And for the other customers that do not have the price formula, it will be arm’s length negotiation.

But I remind you, the purpose for Verallia is to be able, and the goal for the sales team is to cover the inflation of cost factors. In other words, to end up with a positive spread. So if there is a deflation in one country, therefore if in one country the costs are going down, what we want is our prices to go down less than the cost.

Francisco Ruiz: Okay. But as of today, you will say that it is likely not to see our big price decline next year?

Michel Giannuzzi: We do not see a big price decline overall. I repeat, some countries might have a slight price decline because their energy costs are going down much more than others, but in other countries, there is still opportunity to have price increases. So overall, I do not have the numbers yet. We will see at the end of the negotiation where we are not with. But I would say overall it should be more or less flat.

Now regarding hedging, I will let Didier.

Didier Fontaine: Good afternoon. Hedging, you know our strategy on hedging. We do not speculate. We do not keep positions open. Clearly, this has the cost of opportunity and this year if you remember this year, the TTF gas price was at €5 in July this year. Now it is back over €15. So the one who was getting and speculate and kept its book open, benefitted from a lot of advantages, that was not our case. Now we were hedged, that is our strategy. When we go on a negotiation with a customer, we are hedged. And today, we are at a point where we are beginning end of October, beginning of November, we are going to be fully hedged in the coming weeks.

We see the price of the TTF of the gas increasing significantly. So we miss an opportunity, but I said that again, I think you prefer a company like us which is missing an opportunity, then it is taking a little bit hit because it is speculating. So going forward, I have a different view little bit that mid-year really the prices were going down. Now the prices are picking up. I think that it was staying more than €15 the TTF one week ago, so that price continues to increase.

As regards to raw material, I think we have completed on the soda ash. We have diversified our sources of supply, and we have diversified between short-term and medium-term. So we do not foresee a price increase next year on the raw material.

Michel Giannuzzi: Okay. Regarding restructuring, so as you know, we have started a transformation plan in France to adjust our capacity in our French market to a lower level by not rebuilding one of the three furnaces of Cognac factory. This is linked to the fact that the French market is not growing a lot. And what I told you at the beginning of this call is even showing that the French winemakers, for example, are even losing market shares at export.

So this has led us to consider that we did not need so many furnaces in France. And therefore, the furnace in Cognac that was due for reconstruction next year will not be reconstructed. Having said that, we are currently reconstructing one of the other two furnaces. So we are still investing in this region and especially in the Cognac area for that reason.

The purpose of the transformation plan, just to remind everyone, was of course, to eliminate this extra capacity from the French market, which has a direct impact on 80 jobs in Cognac factory. And there was also a change in the organisation in the other factories, the other six factories in order to make them organised the same way as we have in the rest of the Group, which is much more empowerment and much more responsibilisation for the shopfloor, for people. And this was going to lead to additional seven jobs being eliminated in the other six factories.

Verallia being a very responsible company, every effort has been put to negotiate with our union representatives' conditions that will favour early retirement or measures to allow people to set up their own businesses. And in any case, try to avoid as much as possible forcing people to leave the company. In other words, in finding measures that will favour, if you want, voluntary departures.

So we have gone through all the negotiations, all the discussions with our partners, social partners and those negotiations have ended up at the beginning of October. We have now completed all the files that have been now submitted to the French administration for approval of our plan. And that was done on time, which I think was quite remarkable when you know the way that usually those matters are dealt with in France. And we expect an answer from the administration next month.

And hopefully, should this answer be, as expected, positive by getting our plan, this plan should be put in place by the end of the year, beginning of next year. So that is where we are. So we are perfectly in line with our timing, with our planning and also in terms of cost. I remind you that we took a €19 million provision in the first semester to cover for all these plans, including some few asset impairments. So it is not just social cost.

So to summarise, we are well on track on this project of transforming the French organisation and making it at the right level of capacity and also more efficient in terms of organisation.

Regarding your last point, the two new brownfield furnaces in Italy and Spain. As you know, we have postponed the start-up of those two furnaces to next year. I mentioned that we will start them in the first half of next year when we think we need them, and these, I remind you that these are solely dedicated for their domestic markets. In other words, they are not conversely to what some journalists could have said, these are not furnaces that have been built to export to France, to compensate for the closure and the non-reconstruction of the Cognac furnace.

But these are furnaces that are dedicated to the domestic market in Spain and Italy, respectively. So we are all ready to fire them up next year, of course, based on the assumption that next year economy will be steadily recovering from this.

Paul Bradley (Citi): Firstly, I would add my congratulations on this great set of results. Well done. I have got a couple of questions. But first just want to make sure I understand the pricing and cost commentary you have just given. Overall, you expect to see prices at the moment with more or less flat into next year. And from a raw materials point of view also more or less flat into next year. So just to confirm, I understood that correctly.

Michel Giannuzzi: All in that are right assumptions. Right now, I mean, if you mix the 11 countries in which we are if you look at all the cost factors, some cost factors are in some countries down, but others are up. For example, Didier mentioned that, for example, soda ash was probably stable or down in some countries, but labour cost is sometimes up in other countries.

So all in, and including all the countries we are in, it is going to be around zero inflation and around zero price increase. What we want is to end up with a slightly positive spread.

Paul Bradley: Perfect. And on your performance action programme, again, some very good performance in the nine months, so 2.3%. It was 2.6% at the half-year, I think. What should we expect in the full year? You said we were going to get about 2.3% or so or will the fourth quarter sort of tail off as the third quarter has? And what should we be thinking about in terms of next year's performance from the performance action plan? So we said we are sort of 2% or if you are looking again to overdeliver?

Michel Giannuzzi: So on this one, clearly for the full year as also for next year, the goal is more than 2%. Now of course if there is a slow down during the year, you have to incur more industrial variances, because the 2% is net of industrial variances. So if you look at the bridge that Didier has presented, actually the gross PAP is higher – is €36 million and the net is €28 million. So we have got €8 million of industrial variances.

A big part of it is related to COVID, where we have inefficiencies due to COVID, especially in the second quarter. But altogether we are aiming at more than 2% net-net productivity for the full year this year and same thing next year.

Paul Bradley: That is great, thank you. And just finally on the business itself. You have highlighted a couple of innovations you have made. What do you see in terms of customer appetite this year for new products, new innovations, particularly driven by sustainability considerations? I know it has been a funny year and a lot of things probably went on hold in the second quarter. I just wonder if the appetite for new sustainable products or new sustainable angle have come back at all in the third quarter?

Michel Giannuzzi: Well, I think it is a very interesting question. Thank you very much for asking it. We have 10,000 customers. And let us be honest, we have some very small customers that are struggling and frankly speaking they are not thinking about innovation. They are struggling for life. So the small vineyards that we are exporting, for example, to the US and France and that are longer exporting so much or some of them are in difficulty and frankly speaking innovation is not on the top of the agenda.

On the opposite, we have some especially large customers that are still very committed to improving their environmental footprint, improving their CSR performance. And that are strongly interested in any kind of innovation, especially when it is eco-design or eco-innovation that helps them meet their own CSR objectives.

And I have given you some examples here, but we have got plenty of examples of other very large companies that big names, big brands that have not paused this year, despite COVID, on innovation related to carbon footprint and CO_2 emissions. So it is a mixed bag, but with 10,000 customers you can imagine we have all kinds of situations. But clearly, the trend that we mentioned several times in favour of glass is reinforced day after day.

I mean, I gave you today two examples where PET is being substituted by glass. We just have received some interesting statistics from Germany for example where the share of reusable glass for mineral water in Germany has increased in 2020 versus 2019 by five points from 30% to 35% of the containers being used for mineral water.

So this is in one year I think a significant shift. Now clearly the German consumers are probably more eco-conscious than other countries in the world. But this is something we can see in many other countries as well, probably not to the same extent but certainly, the trend is there.

Paul Bradley: Great, thank you, and good luck to you, Didier, on your new ventures.

Didier Fontaine: Thank you very much.

Concluding Comments

Michel Giannuzzi: So thank you very much all of you for attending this call and for following up Verallia. On behalf of the company, I am in front of you because you have been working and interacting a lot with Didier during those years. I would like to thank Didier for his great contribution to these outstanding results and also welcome Nathalie that has been very well-groomed by Didier, as I mentioned before. And I am sure you will be very pleased to meet Nathalie in person as soon as we will be able to physically meet. But I am sure in the short-term, you will see her either through video conferences or in calls.

So thank you very much. And I wish you all to stay safe, healthy and look forward to talking to you again in a few weeks. Thank you.

[END OF TRANSCRIPT]