

16-Aug-2023

West Pharmaceutical Services, Inc. (WST)

UBS Genomics 2.0 and MedTech Innovations Summit

CORPORATE PARTICIPANTS

Eric Mark Green

Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.

Quintin Lai

Vice President-Strategy & Investor Relations, West Pharmaceutical Services, Inc.

OTHER PARTICIPANTS

John Newton Sourbeer

Analyst, UBS Securities LLC

MANAGEMENT DISCUSSION SECTION

John Newton Sourbeer

Analyst, UBS Securities LLC

So thanks, welcome to the UBS 2023 Conference here. I'm John Sourbeer, UBS' life science analyst. Happy to host the fireside today with West Pharmaceutical. Joining me is CEO and President, Eric Green; and VP of Investor Relations, Quin Lai.

Hi. Thanks for attending here.

Eric Mark Green

Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.

Yeah, John. Thanks for having us. It's been a really good day here at UBS. So thank you.

QUESTION AND ANSWER SECTION

John Newton Sourbeer

Analyst, UBS Securities LLC

Q

Great. So maybe start off here high level question. I know you guys reported earnings a couple of weeks ago. But on the demand environment, the company continues to see strong demand really across its proprietary product segment and the broader portfolio despite macro headwinds seen by peers and others within biologics or biopharma life science tools. So I guess, when you look at that demand, how much of this is GLP-1 versus traditional biologics, MABs, and can you just talk about how sustainable is the current demand environment? Maybe, I'll pause there.

Eric Mark Green

Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.

A

Yeah. Thanks, John. I think when we look at the growth of the business, it's really kind of break it down in two components; one, let's take COVID out of the picture. As you know, we had significant participation during the pandemic, but the core business itself, the base business has been growing double-digits since early 2019 consistently on a quarterly basis. And it's really driven by a couple of key areas, number one is from the biologics that continues to be the fastest area of growth for West, and our participation rate remains very high in that particular space. That also includes biosimilars. And we're also seeing good growth in all of our pharma and in our generics business. In fact, generics has been growing quite faster than what we'd say about the long-term construct.

So the business has been growing strong double-digits for quite a while. However, when we think about high single-digit growth for West, we're really think about long-term growth algorithm of 7% to 9%. And the way to break that down is, think about double-digit growth for biologics. Generics we believe it's mid- to high single-digits for West. And then pharma, which is innovative molecule sector, is low to medium. And their contract manufacturing business, which is about 17% or 18% of our business, is growing, we believe, long-term construct is mid to high single-digit. So when you roll that together, it gets you that 7% to 9% long-term construct, which we have been exceeding over the last few years, which is positive.

John Newton Sourbeer

Analyst, UBS Securities LLC

Q

And maybe, just because you touched on it, I'll ask this great question, maybe piece of time to ask this. But the contract manufacturing, you did I think maybe two quarters ago increased the construct there. And even with that increasing, are you still thinking 7% to 9% long term is the sustainable growth for the business?

Eric Mark Green

Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.

A

Yeah. For overall enterprise, a few years ago, contract manufacturing was a larger portion of our overall enterprise, and that's come down to about 17% to 18%. So we do believe mid to high single-digit growth is what we'll see with contract manufacturing, more long term, I realized this year we're good solid double-digit growth, that's due to learning capital we put in last year that is now up and running and commercialized today. So long-term mid to high single is our corridor with the contract manufacturing.

John Newton Sourbeer*Analyst, UBS Securities LLC*

Q

Great. And you just typically don't talk about specific customer types, but there's lots of discussions about GLP-1. So I'll try to asking here another question on this. But any color just how you see this evolving, there's some oral GLP-1 that could potentially come to market. How does this new maybe impact the larger demand, 10% to 20% of these products shifting to oral is the right way to think about it? And I guess, when you look into your demand algorithm, how should we think about that?

Quintin Lai*Vice President-Strategy & Investor Relations, West Pharmaceutical Services, Inc.*

A

So I think, you're right. I mean, we try to refrain from talking about any specific disease or drug category. So look, all things being equal and they rarely are, drug companies, patients typically prefer oral. But then there is a reason why injectables are growing because the effectiveness, the bioavailability, the amount of API required per dose to get that whatever effect that they're looking for, trying to balance that versus potential side effects, all of those things come into play. And so I think that all of those discussions have to come in, which is why we always refer those type of questions on the specific to the drug company, because really they monitor and make those decisions.

What we do is, we talk with all of our customers. Because of our position and our leadership, we share with them our expansion plans. Some things take time to build up capacity. And on the flip side, what we ask of them is to get visibility on their near, mid and long term expectations. And for customers that have larger launches or larger expectations, the touch points are more frequent. And we're always adding that as we're trying to do our capacity planning. And so what we've said and been fairly consistent here over the last couple of years is that, we are adding HVP capacity as there has been a particular focus on plungers. And just recently we brought on line in one of our centers of excellence in the United States, our Kinston, North Carolina plant, NovaPure plunger capacity.

John Newton Sourbeer*Analyst, UBS Securities LLC*

Q

Right. And I want to dig in all those pieces, so maybe just one last I want to hear that. So I think broadly speaking, you're in about 90% of the biologic filings. Any thoughts just on market share, how that is, maybe even GLP-1s or other products there on that piece?

Quintin Lai*Vice President-Strategy & Investor Relations, West Pharmaceutical Services, Inc.*

A

Sure. The way we track it is our participation rate. We really focus on our partner Daikyo, and how we're tracking with respect to NMEs, new molecular entity approvals. And if you look at year-to-date, if you look at last year, if you look over the last five years, it's a really high participation rate. And we think that that is probably a good proxy for market participation.

John Newton Sourbeer*Analyst, UBS Securities LLC*

Q

Okay. So moving beyond the GLP-1s, and you guys just reported the nice 2Q earnings. I guess, just how should we think about the revenue cadence for the remainder of the year, between the two quarters I know you have gave some dynamics, perhaps becoming on line, COVID rolling off, how do you just think about that?

Eric Mark Green

Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.

A

Well, I think, take a look at – we believe the second half will be greater than the first half. And we have historically seen seasonality of our business where Q2 tends to be the largest quarter. Q3 is less, and then it kind of reverts back to a higher level in Q4. That seasonality still exists as we look at 2023. However, we do have some, as Quintin indicated earlier, investments that we've been making. One in particular is in Kinston, North Carolina with NovaPure plungers, that as where we sit today, as I'm speaking, we are ramping up on commercial manufacturing and supporting our customers. There is demand for the products. That's why, obviously, we put the investments in, and we believe that plus, getting our lead times back in line to pre-pandemic levels, which we believe will take till the end of this year, will give us stronger performance in Q3 due to that. It's going to offset the seasonality. So the way I would look at is Q3 to be similar plus or minus to Q2. Then Q4 will be stronger, therefore the second half will be stronger for us.

John Newton Sourbeer

Analyst, UBS Securities LLC

Q

[indiscernible] (00:08:38), with the capacity coming on line, and I guess specifically Kinston. Anyway, I think you mentioned, so just to clarify, is that doubling your NovaPure capacity, once that would be fully on line or how should we think about that?

Eric Mark Green

Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.

A

In that NovaPure, in general, but around our NovaPure plungers at that site, so it gives us significant expansion. The way that we made the investment is that, we have the infrastructure expanded, the modular approach. We have installed new equipment and technology to produce the product with new team members on-site. If demand continues to accelerate, we were able to install additional equipment without other infrastructure required. So I think, we really purposely did a really good job on staging the investments, and as we go forward to stay ahead of the curve versus getting behind it like we were in the last year or two. So really confident. We're positioned well now for NovaPure plungers.

John Newton Sourbeer

Analyst, UBS Securities LLC

Q

Great. And then just maybe broader capacity as you also have Jersey Shore, Pennsylvania and Singapore, you mentioned, just any additional color and just like I guess on the demand you're seeing and maybe how much is committed or any way to quantify that?

Eric Mark Green

Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.

A

The way I would look at it, this year we've committed to about \$350 million of capital, which is, if you think about it as a percentage of sales, it's higher than we've articulated in the past. We were looking at about 6% to 7% of sales for capital, for a business growing about 7% to 9% organic top line. What we're seeing today, as the \$350 million, like we saw last year, is that about 70% of those investments is around growth. I think historically at West we were about 50/50, 50% in growth, about 50% on maintenance and IT. We're seeing heavier emphasis on growth which is a good thing. It means that we are working with our customers, anticipating additional launches in the near to mid-term time horizon.

So we are making investments. It's not just in Kinston. These investments take one to one-and-a-half years from a modular point of view. We're making investments in our Waterford facility as we speak, in Jersey Shore in

Pennsylvania, also significant investments in Singapore, which is a great manufacturing platform for us, for all of Asia, but able to export it outside of Asia. So it gives us the ability to support the growth that we're seeing with high value products. It is disproportionately investments are around plungers, not just NovaPure, but other types of formulations to be able to support growth that we're seeing in the biologics and other areas of the markets. So we're excited with these investments. There's multiple moving parts, but that's a good thing for us as we continue to look for growth in our organization.

Quintin Lai*Vice President-Strategy & Investor Relations, West Pharmaceutical Services, Inc.*

A

Let me add a little bit to that. I mean, it kind of underscores the fact that we don't have really high concentration either to a single customer or single drug class and the growth that we've been seeing since 2019 has been fairly widespread. And so the capacity that we're adding enables West [indiscernible] (00:11:57) our quality, our SRU. It helps envision capabilities. It works on at the floor tech level as well as the high profile NovaPure that we talk about. So a lot of the attention gets put on to just Kinston, but we have a lot of efforts and a lot of projects going on throughout our network. Even in some of our standard areas we have projects going on. So we have a very robust CapEx expansion right now going on.

John Newton Sourbeer*Analyst, UBS Securities LLC*

Q

Thanks. And I guess, just with that robust CapEx expansion and you've talked about this larger demand, but I guess even within HVP capacity that you're bringing on or just broader current capacity, any color on what products you're seeing the most demand there within your portfolio?

Eric Mark Green*Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.*

A

As Quintin mentioned, it's really across the whole portfolio, and it does show the robustness of how we're penetrating into the pharma, the generics and also in the biologics. I'd be remiss if I didn't say we are continuing to add capacity in contract manufacturing. But these are very long-term agreements. Our customers are also installing capital in these investments. So it's a joint long-term relationship. So it is across the spectrum. But I would argue that most of the investments are more of the higher end of HVP, which is positive because as you know, we've been seeding the market, where we win is in the pipelines, and we continue to see the market with the highest end of our high-value products. We're seeing the high participation rate across the board, which is exciting. And we're preparing ourselves with customer conversations of additional launches that we're looking at that are on us today and also into 2024.

John Newton Sourbeer*Analyst, UBS Securities LLC*

Q

Thanks. And HVPs are roughly about 73% mixed today. I think you ended the year at 72% last year. Just any color on where you see the possibility for the penetration to go here, and then what would be the dynamics or maybe top line or bottom line impact from that?

Eric Mark Green*Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.*

A

We see HVP growth continue to be strong double-digits. We see the key drivers of the growth really is in the biologics, the biosimilars space. We're also seeing greater penetration in generics, and that is leveraging our [indiscernible] (00:14:27) and other parts of our portfolio in HVP. So we're quite confident in our growth profile of high value products, which is actually quite exciting. So we'll continue to invest in those areas. But it is kind of

across multiple markets, multiple drug molecules, multiple customers and multiple geographies where we're seeing the penetration continue to stay very high in that area.

John Newton Sourbeer

Analyst, UBS Securities LLC

Q

And I guess just maybe back to another question, just on the seasonality in the second half, I believe that you mentioned that you're not seeing the normal plant shutdowns this year for different maintenance with the capacity coming on line. Just any way to run through the color there on that?

Eric Mark Green

Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.

A

Well, I'll start with this. We are still shutting down plants in certain parts like in Europe to make sure that we are managing the maintenance because that's so critical to keep our level of quality that we are producing each and every day and our customers are accustomed to. So that is important for us to continue to do so. We do have larger vacation times, I guess, you could call it, in Europe at this time of the year. But so we're not pulling back on our maintenance and shutdowns other than we have installed capacity that is ramping up to offset that this year and particularly in Kinston and a couple of other locations. So that's how, it's the puts and takes, and I think overall it brings it to a higher level than we would have anticipated last year or the year before. But yes, definitely continue with the maintenance and the investments in those areas.

John Newton Sourbeer

Analyst, UBS Securities LLC

Q

Thanks. And GLPs get a lot of talk, but another area for driving that high single-digit growth you talked about have been biosimilars. Just any additional color on how you see biosimilars continue to impact the market there, maybe near term or long term, maybe pause there and then I'll follow-up on this.

Eric Mark Green

Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.

A

We still have a very strong participation rate in biosimilars like we do in biologics. But from a value proposition, our portfolio, our technology jointly with Daikyo really resonates well with our customers in both areas because of the way it is able to support the molecule as they launch. So we're excited about the biosimilars as much as we are with the biologics. We're well-positioned. It's on a different product category for West. It's a similar value proposition, similar products that we are producing such as NovaPure from our existing lines. We don't have to have any dedicated equipment for any particular customers or launches. So it fits really well for business model, and we're excited with the growth opportunities of biosimilars as we are with the biologics.

John Newton Sourbeer

Analyst, UBS Securities LLC

Q

And you kind of touch on there on the end. But if you're not seeing a non-HPP product in the originator or it was transitioned, usually do you come in then on the biosimilar, would it be an HVP product, like what level of HVP, any color on that?

Eric Mark Green

Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.

A

Yes. So you're right. When we think about NovaPure, the journey of NovaPure, we really launched that in call it 2016 and beyond. So many of the molecules that may have improved in on the market and commercialized prior

to that would not be leveraging NovaPure for the most part. As customers are looking to transition to a biosimilar, the discussions we have with our customers start with NovaPure, as in any other pipeline of opportunity. And so there is that transition, a mix effect that's going to occur within our HVPs because of that effect. As biosimilars are being approved, we're seeing a higher leverage in the usage of our NovaPure portfolio.

John Newton Sourbeer*Analyst, UBS Securities LLC*

Q

And then, I guess, just on pricing. I think you're targeting still this year 5% to 6% pricing increases. Just any thoughts long term and how the sustainability of the pricing you've been able to capture here?

Eric Mark Green*Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.*

A

All right.

Quintin Lai*Vice President-Strategy & Investor Relations, West Pharmaceutical Services, Inc.*

A

Yeah. So let's kind of start with historically a few years ago, the company would get about 1% to 2% price per year, often at the lower end of that range. We have talked about looking at price more strategically, and we have brought in teams to look at that. And over the last few years, I believe we have been more strategic on pricing to be a little bit better than what that historical range has been. Then you couple it with the inflation pressures that have occurred for not just us, but the whole economy over the last couple of years. And we've been able to then take that and be able to use that structure that we have with pricing to be able to help offset some of the inflationary costs that are coming in.

So, this year, what we had said is that it is going to be 5% to 6%. That is markedly higher than where it has been. But we're also experiencing inflationary issues in some materials, some supplies, some utilities, but in particular, labor because of the labor demands here over the last two years. And so, that has driven us to where we are. We haven't given any forward guidance on where it could go. But again, I'll just leave it as that that, we continue to believe that we can continue to be more strategic, certainly than the historical 1% to 2%.

John Newton Sourbeer*Analyst, UBS Securities LLC*

Q

And Eric, you touched on this a little bit in the beginning, just in the overview on demand market. But, you recently increased the contract manufacturing piece to that mid-single-digit, high-single digit growth there. Just any additional color on what drove the increase in your outlook and execution for that segment of your business?

Eric Mark Green*Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.*

A

It's these long-term agreements that we're signing and starting to invest in. So, we do have visibility. That's one part of the business where the installed equipment, new facilities are really dedicated to a particular product and a customer. And these are very long-term, i.e., five, seven-plus year agreements. And so, with that being layered in and knowing that we are – we'll be turning those on and the requirement is get to close to 100% utilization as soon as possible. This is pretty good confidence of moving that up between mid to high single digits more longer term.

The particular area around auto injectors is probably the biggest driver. When you think about the injectable in medicine space we participate, the number of auto injectors, but that's probably the biggest area of growth we're seeing right now in CM.

John Newton Sourbeer*Analyst, UBS Securities LLC*

Q

And maybe moving through a little bit below the line and some of the impact on the HVPs there. Could you just remind us the impact on HVPs on margin versus maybe non-margin mix and any way just to quantify that, let's say every 100 bps increase, how that impacts HVPs on margins? Just how should we say like every 100 bps of penetration increase there and maybe the thoughts on that?

Eric Mark Green*Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.*

A

Yeah. Again, so a couple of things there. I think that wouldn't – you have a top line of 7% to 9% of construct organic sales consolidated that presumes that HVPs are growing north of that and the standard product scoring less than that. So, let's get away from percent of sales. Let's just look at the drivers plus or minus to that.

And so when HVPs are growing in the double digits, given their margin profile, yeah, the construct would yield about a 70 bps to 80 bps per year of gross margin improvement. And then with other operational efficiencies plus a little leverage on SG&A per year, then that gets us to the 100 bps plus per year construct. So, nothing has changed. You're absolutely correct. HVPs are going to be the driver of top line as well as gross and operating margin expansion.

John Newton Sourbeer*Analyst, UBS Securities LLC*

Q

Thanks. And maybe just now switching to some of the more macro near term, any updates on Pfizer, the situation in Rocky Mount with recent storms there? Luckily no one was hurt. But any just thoughts on the broader impact and any updates [ph] since (00:23:22) the quarter there on that?

Eric Mark Green*Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.*

A

Yeah, it's just devastating to see what impact it had at that site. And so, we reached out immediately afterwards. As you know, we have our own facility, Kinston, North Carolina. It's about 50 miles or so from their location. So, our teams know each other very well and we reached out – [ph] do kind of (00:23:41) what we can do to support them in any given way. I think the whole supply chain is ready to react, to build support in a meaningful way to make sure that there isn't a disruption for them. But, yeah, it's more – we'll see more as we go down the road and we're ready to respond.

John Newton Sourbeer*Analyst, UBS Securities LLC*

Q

Thanks. And any color just on – we've seen some destocking from those life science tools companies better facing with biologic customers, just how are you seeing any impact from that?

Eric Mark Green*Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.*

A

What we're seeing in the working capital or working management, capital management, when you think about, obviously, COVID is an area we're seeing destocking. And last year, we did about \$388 million of COVID-related materials, and this year it's going to be – we're forecasting about \$60 million. So there's an effect there. We are seeing some destocking in areas around the disposal medical devices or call it standard products. For us, it's another area. We tend to see a little bit of this happening.

But these amounts are not material to us. We're able to manage through that, work with our customers, keep our operating facilities in check. If it will have an impact on site, we will do work with our customers. For the most part, we think about during the COVID time period, we were getting behind our lead times. And so, many of our customers, safety stock levels, did not get escalated or get larger than they anticipated during the pandemic. [ph] And so (00:25:19) we're actually in a good place right now where our lead times to get a little bit large. We brought them in. We're working down the need for additional materials with our customers. So right now, where we stand what we see is not a lot destocking with our products.

John Newton Sourbeer

Analyst, UBS Securities LLC

Q

Thanks and I guess, while we're on the near-term and the macro, I think China is a small portion of your revenues. But can you remind us what the exposure is there and any color on the outlook for the China market?

Eric Mark Green

Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.

A

I'll cover that. Yeah. So, I think it's a small percentage of our business. We do have two manufacturing plants in Qingpu just outside of Shanghai that will supports the local market with certain product portfolio that's focused on that area. We actually are seeing good growth outside of COVID. That's another part of the world where we're seeing a decline in COVID. But net-net, we're seeing relatively neutral.

We're not seeing a reduction. Our reliance on raw materials coming out of there is less. A lot of our sourcing of our materials are really co-located with our manufacturing plants – on the continents. So we have less risk in those areas. But it's a small piece of our business, so it's really not material. We haven't really called it out. And frankly, we're not seeing a big change on the demand profile in China for us today.

Quintin Lai

Vice President-Strategy & Investor Relations, West Pharmaceutical Services, Inc.

A

Yeah. So John, as a reminder, I mean, our exposure in China as well as the rest of the world is mostly on commercial volumes. We do sell some to customers that are doing preclinical and clinical trials. But that volume is small relative to the rest of the business. And we don't have really any sales to speak of at the discovery level. And so, to compare and contrast with other life science tools companies.

John Newton Sourbeer

Analyst, UBS Securities LLC

Q

That's great, [indiscernible] (00:27:17) next question, West is very highly levered to those commercial revenues. Any just impact you've seen from, obviously funding or even slowing of R&D from pharma customers? Has that impacted the business at all?

Eric Mark Green

Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.

A

No. No, it hasn't. As we mentioned earlier, our success really is in the pipeline, so you're right. It's an important area that we focused on. But the – from a revenue and profit perspective, it's very small minimal impact. These volumes are very limited. We are [ph] ceded (00:27:52) in the markets with Ready Pack and other materials, but it's really meaningful when it gets in the commercial stages. So, today we do believe the engine of innovation continues to thrive and we'll continue to support it short-term and mid-term.

John Newton Sourbeer*Analyst, UBS Securities LLC*

Q

And maybe just last one on COVID while we're here, just you've cut COVID guidance this year. When you look at now two quarters in, any way to think about the endemic run rate from here and just where COVID – you see the tracking from here?

Quintin Lai*Vice President-Strategy & Investor Relations, West Pharmaceutical Services, Inc.*

A

Yeah. I mean – look, I mean, I think we all along with all of society are hoping that we are getting to a – this lower phase and kind of situation with COVID. So, for the back half of the year, the expectations are really small in terms of our COVID sales. And as Eric says, we definitely have seen destocking in that area. In the event that the pandemic rears up again, and if there is a need for vaccines and treatments, we'll be ready and that is our commitment, we will be there. But right now, nothing to add.

John Newton Sourbeer*Analyst, UBS Securities LLC*

Q

Thanks. And I wanted to ask one on the Corning collaboration and the West Ready Pack, the Corning Valor. Just any color on demand there and just how this could potentially play out increased demand on HVPs or NovaPure?

Eric Mark Green*Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.*

A

Yeah. It's an exciting area of investment that we're making – working with Corning. The concept there is that we do believe that there's a drive towards integrated systems. And the elastomer component is a critical element of any type of system, whether you're talking about a cartridge or a prefilled syringe. And working with Corning gives us the ability to bringing the glass element, which we currently do not have. So, we're excited. We've had a couple of launches around the vial configuration, and we'll continue to work all the way up to a fully characterized prefilled syringe in the near future.

Our focus is really, again to see the market and then bring the demand in through new approvals. But we're in a very unique position with that relationship to ultimately get to what we believe the one drug master file approval approach with our customers, which is resonating very well in the market today. The question is, how fast can we go? And so, we're deliberately – we're working swiftly with our – internally both at Corning and at West, but also with our customers. So, we'll – more to come, but it's very early at this point in time.

John Newton Sourbeer*Analyst, UBS Securities LLC*

Q

I guess just broader on that and moving to that the one product approval, just any changes in the competitive dynamics in the broader industry that you've noticed now that we're exiting the COVID pandemic?

Eric Mark Green

Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.

A

Look, we have really formidable, competitors in the marketplace, really good company that's well run. We don't see ourselves, we don't see a change in the dynamics of market share, in particular. We do monitor very closely what we call participation rate of new approvals. And we continue to have very high acceptance of biologics, obviously, other enemies in the small molecule area and also seen a little tick-up in the ANDAs or the generics area. So – but we don't – from our lens and our position, we don't see any major shift at this point particularly on our elastomers – of our business.

John Newton Sourbeer

Analyst, UBS Securities LLC

Q

And question we have here and from the audience, [indiscernible] (00:31:43). As your lead times are returning back to those normalized level, can you speak into any of the visibility into customer inventories or other metrics that might insulate West from lower ordering patterns which have come up in other parts of the pharma manufacturing chain?

Eric Mark Green

Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.

A

Yeah. So, one encouraging area is that because we're bringing the lead times down customers are getting more confident in shorter lead times, therefore we're having more frequent, more near-term orders versus very elongated one, two years out type of approach. That's where we wanted to get to. So it allows us to be more flexible with our operations. It allows us to be more responsive to our customers' needs, allows them our customers to not have to build significant levels of safety stock.

And so, we're in a much better position today and the visibility remains – continues to remain very high. We do interact with our customers frequently on not just current drug molecules in the marketplace, but also planning for future launches for near- and mid-term, because sometimes we will have to make investments in advance to make sure that we can handle the volumes that will be asked upon us. So, the lens is very good for us and we continue to build off of that. I think that's been one of the biggest changes we made in this organization over the last five or six years, which is really paying off today.

John Newton Sourbeer

Analyst, UBS Securities LLC

Q

I guess, have you quantified what lead times are now, let's say, where they were prior to the pandemic 2020, 2021? Have they down from maybe months out in ordering?

Quintin Lai

Vice President-Strategy & Investor Relations, West Pharmaceutical Services, Inc.

A

So, it varies by SKUs, we had some certain HVP categories that the lead times exceeded 40 weeks. And what we'd like – we would rather see in some of those cases to be between 10 weeks to 14 weeks, maybe sometime between 8 weeks to 10 weeks. And so, our expectation now is that as we've been bringing on HVP processing capacity, and that began last year and into this year as we brought in now more plunger capacity and NovaPure capacity, that by the end of the year the majority of our portfolio will be getting back to more normalized lead times.

John Newton Sourbeer

Analyst, UBS Securities LLC

Q

Thanks. And we touched on lots of different parts of business. One we haven't talked on is the generic segment. Just any color there on the year-to-date performance and outlook in the second half?

Quintin Lai

Vice President-Strategy & Investor Relations, West Pharmaceutical Services, Inc.

A

Yeah. So, yeah, I think generics has been really – so, if you look at it excluding COVID-19 impact, it has been really strong double-digit growth in generics. Part of that has been benefited from the fact that we've been able to work some of the lead times down and bring up the safety stocks. And so, certainly these long lead time items that [indiscernible] (00:34:48) stocks are being replenished. So – and then the rest of the underlying growth continues to be good because the volumes have been good, the number of ANDAs in our participation rate have been good and the conversion of some of these customers moving to like a Westar RU format or Ready-to-Use format have been good and that – those have all been drivers. So, it's kind of a combination of all three.

John Newton Sourbeer

Analyst, UBS Securities LLC

Q

Great. Anyhow we're reaching about time here. Just last question, maybe just more, Quintin, follow-up on the margin piece. Can you just run through on just I guess we talked to the top line cadence second half just on how margins should track. It's really tracking in line with [audio gap] (00:35:34) the dynamics of capacity coming online and any thoughts there on that?

Quintin Lai

Vice President-Strategy & Investor Relations, West Pharmaceutical Services, Inc.

A

Yeah. So look, if you look at it from a typical seasonality and if you look at a typical West year, which has been a long time since we had a typical West year with COVID going up, coming down, all that. The second quarter typically is our largest sales quarter. It would typically is our best gross margin quarter because it's also the – we have great utilization, more uptime, good absorption. The lowest quarter typically is Q3 because of the summer shutdown, especially in Europe and Q4 is the second lowest.

So, those dynamics of the seasonality will continue, but the drop in gross margins will not be as dramatic as in prior years because we are bringing on capacity for HVP. The implications in our guidance is that capacity is going to come on at nice incremental margins, but not the full contribution margin given the fact that it's a new facility and you always have startup costs with the facility. So that is the net-net of why sales will be plus or minus where Q2 are better than Q4, but margins will be just a tad less than what we saw in Q2.

John Newton Sourbeer

Analyst, UBS Securities LLC

Great. Well, I think that's a great place to end the conversation. Eric and Quintin, thank you very much for joining us today and thank you for those in the audience and listening in.

Eric Mark Green

Chairman, President & Chief Executive Officer, West Pharmaceutical Services, Inc.

Thank you very much for having us. Thanks.

Disclaimer

The information herein is based on sources we believe to be reliable but is not guaranteed by us and does not purport to be a complete or error-free statement or summary of the available data. As such, we do not warrant, endorse or guarantee the completeness, accuracy, integrity, or timeliness of the information. You must evaluate, and bear all risks associated with, the use of any information provided hereunder, including any reliance on the accuracy, completeness, safety or usefulness of such information. This information is not intended to be used as the primary basis of investment decisions. It should not be construed as advice designed to meet the particular investment needs of any investor. This report is published solely for information purposes, and is not to be construed as financial or other advice or as an offer to sell or the solicitation of an offer to buy any security in any state where such an offer or solicitation would be illegal. Any information expressed herein on this date is subject to change without notice. Any opinions or assertions contained in this information do not represent the opinions or beliefs of FactSet CallStreet, LLC. FactSet CallStreet, LLC, or one or more of its employees, including the writer of this report, may have a position in any of the securities discussed herein.

THE INFORMATION PROVIDED TO YOU HEREUNDER IS PROVIDED "AS IS," AND TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, FactSet CallStreet, LLC AND ITS LICENSORS, BUSINESS ASSOCIATES AND SUPPLIERS DISCLAIM ALL WARRANTIES WITH RESPECT TO THE SAME, EXPRESS, IMPLIED AND STATUTORY, INCLUDING WITHOUT LIMITATION ANY IMPLIED WARRANTIES OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, ACCURACY, COMPLETENESS, AND NON-INFRINGEMENT. TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, NEITHER FACTSET CALLSTREET, LLC NOR ITS OFFICERS, MEMBERS, DIRECTORS, PARTNERS, AFFILIATES, BUSINESS ASSOCIATES, LICENSORS OR SUPPLIERS WILL BE LIABLE FOR ANY INDIRECT, INCIDENTAL, SPECIAL, CONSEQUENTIAL OR PUNITIVE DAMAGES, INCLUDING WITHOUT LIMITATION DAMAGES FOR LOST PROFITS OR REVENUES, GOODWILL, WORK STOPPAGE, SECURITY BREACHES, VIRUSES, COMPUTER FAILURE OR MALFUNCTION, USE, DATA OR OTHER INTANGIBLE LOSSES OR COMMERCIAL DAMAGES, EVEN IF ANY OF SUCH PARTIES IS ADVISED OF THE POSSIBILITY OF SUCH LOSSES, ARISING UNDER OR IN CONNECTION WITH THE INFORMATION PROVIDED HEREIN OR ANY OTHER SUBJECT MATTER HEREOF.

The contents and appearance of this report are Copyrighted FactSet CallStreet, LLC 2023 CallStreet and FactSet CallStreet, LLC are trademarks and service marks of FactSet CallStreet, LLC. All other trademarks mentioned are trademarks of their respective companies. All rights reserved.