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West Pharmaceutical Services, Inc. (WST)

Q1 2022 Earnings Call

CORPORATE PARTICIPANTS

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MANAGEMENT DISCUSSION SECTION

Operator: Good day and thank you for standing by. Welcome to the Q1 West Pharmaceutical Services Earnings Conference Call. At this time, all participants are in a listen-only mode. After the speaker presentation, there will be a question-and-answer session. Please be advised that today's conference is being recorded. [Operator Instructions] I would now like to turn the conference over to your speaker today, Quintin Lai, Vice President of Investor Relations. Please go ahead.

Quintin John Lai

Vice President-Corporate Development, Strategy and Investor Relations, West Pharmaceutical Services, Inc.

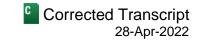
Thank you, Debbie. Good morning and welcome to West's first quarter 2022 conference call. We issued our financial results this morning, and the release has been posted in the Investors section on the company's website located at westpharma.com.

This morning, CEO, Eric Green; and CFO, Bernard Birkett, will review our financial results, provide an update on our business, and present an update on our financial outlook for the full year of 2022. There's a slide presentation that accompanies today's call, and a copy of that presentation is available on the Investors section of our website.

On slide 4 is our Safe Harbor statement. Statements made by management on this call and in the accompanying presentation contain forward-looking statements within the meaning of US federal securities law. These statements are based on our beliefs and assumptions, current expectations, estimates and forecasts.

Future results are influenced by many factors beyond the control of the company. Actual results could differ materially from past results, as well as those expressed or implied in any forward-looking statement made here.

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Please refer to today's press release, as well as any other disclosures made by the company regarding the risk to which it is subject, including our 10-K, 10-Q and 8-K reports.

During today's call, management will make reference to non-GAAP financial measures, including: organic sales growth, adjusted operating profit, adjusted operating profit margin, and adjusted diluted EPS. Reconciliations and limitations of the non-GAAP financial measures to the most comparable financial results prepared in conformity to GAAP are provided in this morning's earnings release.

I now turn the call over to West CEO and President, Eric Green. Eric.

Eric Mark Green

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

Thank you, Quintin, and good morning, everyone. Thanks for joining us today. We will start on slide 5. I'm pleased to report that we delivered a strong first quarter. This was driven by double-digit organic sales growth with increase in demand for our high-value products. Our confirmed order book for the rest of 2022 and into 2023 remains as strong as ever, primarily driven by non-COVID based business. And to provide you more color, over half of the order book is coming from biologics demand. These results were delivered despite several macroeconomic challenges that are impacting all companies and sectors.

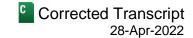
We have taken proactive measures to mitigate the risk of these challenges and ensure the continuity of critical components to our customers. For example, inflation: we're adjusting our pricing strategy and have enacted surcharges as a pass-through to offset increasing costs of raw materials, energy and transportation. Supply chain: our raw material and proprietary medical device components are sourced from across the globe. We have increased our inventory of these key raw materials to minimize any supply disruption. And we continue to execute and monitor our business continuity plans with respect to these issues, including the war in Ukraine and the recent pandemic surge in China.

Turning to slide 6. Our team members across the globe continue to demonstrate their passion to improve patient lives as they remain focused on our strategic initiatives of Execute, Innovate and Grow. Starting with the first pillar of Execute, we continue to deliver the key drivers of growth in Q1 with strong customer demand of HVP components, including NovaPure and Westar. There was solid demand in the quarter across all market units, and a positive outlook remains for the rest of the year. And in particular, for our Biologics market segment, which is now greater than 42% of our total sales, we see both existing and new customers continue to spec our highest level of components by West, or our partner Daikyo for the sensitive molecules.

Our capital [indiscernible] (05:05) investments through expansions and optimizing productivity across our global operations remain on track. To-date, almost all of our 2020 expansion phases have been installed, validated and in production. And we're making good progress on the 2021 capital expansion plans, some of which will come online in the second half of 2022 and throughout 2023. With the accelerated biologics demand for NovaPure, we have executed additional support for NovaPure future demand, as well as other HVP finishing capabilities. Expansion construction is underway and will be online towards the back half of this year with commercial production in 2023.

Shifting to West team of scientific and technical experts, we continue to educate and share insights and biologics, combination products, and container closure integrity, which are our priority areas in pharmaceutical packaging. At the recent PDA Annual Meeting, several of our West experts were recipients of prestigious awards.

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Now to Innovate: We need to fuel innovation to develop future products, solutions and services that connect the dots across science and technology to create customer value. We're doing so by investing in external opportunities that complement our current business needs such as our partnership with Techin to create a research center of excellence in combination with West's scientific expertise. The Corning collaboration, as we expand our HVP value proposition to lead the industry from components, to a truly integrated system of elastomer and glass, and building technologies like the recent collaboration with Pneuma Systems to develop a family of fluid flow technologies for drug delivery. I'm pleased on the progress on – our R&D team is making around Innovate.

Moving to the final pillar, Grow, which includes uses of cash, we're working from a position of strength, as we believe we have a long horizon of continued strong organic sales growth and margin expansion. As we have demonstrated over the past two years, we have increased our capital spending for capacity expansion at existing sites across our global network to support our organic growth initiatives. In addition, we have made inorganic investments such as partnerships with Corning. Our continued focus within these three strategic pillars, Execute, Innovate, and Grow, allows us to be more responsive, leverage our assets more effectively, and support the trends that are happening in the industry today. This was most evident from my recent site visits in Dublin and Waterford, Ireland. For example, in Dublin, I saw firsthand how the digitalization of our manufacturing technologies is providing real-time data, enabling our team to raise the bar in operational performance with higher yields and efficiencies. At Waterford, the capital investments over the last year-and-a-half have significantly increased capacity, with additional lines producing the HVP product to meet increased demand. And we're seeing early success with our next generation, fully integrated automation that we believe will scale and transfer across the network for a combined benefit of higher quality production and higher manufacturing throughput. Lastly and proudly, the hard work of our Waterford team was acknowledged by the Ireland-US Council as we received the Global Public Service Award for our commitment during the pandemic.

Now I'll turn it over to our CFO, Bernard Birkett, who will provide more detail on our financial performance.

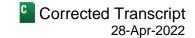
Bernard J. Birkett

Senior Vice President & Chief Financial Officer, West Pharmaceutical Services, Inc.

Thank you, Eric, and good morning. Let's review the numbers in more detail. We'll first look at Q1 2022 revenues and profits where we saw continued strong sales and EPS growth, led by strong revenue performance in our biologics and pharma market units. I will take you through the profit growth we saw in the quarter, as well as some balance sheet takeaways. And finally, we will provide an update to our 2022 guidance.

[ph] First off (09:35), Q1, our financial results are summarized on slide 7 and the reconciliation of non-GAAP measures are described in slides 15 to 18. We recorded net sales of \$720 million, representing organic sales growth of 11%. Looking at slide 8, proprietary product sales grew organically by 14.4% in the quarter. High-value products, which made up approximately 73% of proprietary product sales in the quarter, grew double-digits and had solid momentum across Biologics and Pharma market units in Q1. Looking at the performance of the market units, Biologics market unit delivered strong ,double-digit growth. We continue to work with many biotech and biopharma customers who are using West and Daikyo high-value product offerings. The Generics market unit experienced mid-single digit growth led by sales of FluroTec and Westar components. Our Pharma market unit saw high-single digit growth with sales led by high value products including Daikyo and NovaPure components. And contract manufacturing declined 3.8% for the first quarter due to a reduction in sales of components for diagnostic devices. We recorded \$284.6 million in gross profit, \$12.7 million or 4.7% above Q1 of last year. And our gross profit margin of 39.5% was a 100 basis point decline from the same period last year. We saw improvement in adjusted operating profit, with \$189.9 million recorded this quarter, compared to \$179.2 million in the same period last year, or a 6% increase. However, our adjusted operating profit margin of 26.4% was a 30

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basis point decrease from the same period last year. Finally, adjusted diluted EPS grew 12% for Q1. Excluding stock based compensation tax benefit of \$0.12 in Q1, EPS grew by approximately 15%. So let's review the drivers in both revenue and profit.

On slide 9, we show the contributions to sales growth in the quarter. Volume and mix contributed \$49.9 million or 7.4 percentage points of growth and sales price increases contributed \$23.6 million or 3.5 percentage points of growth in the quarter.

Looking at margin performance, slide 10 shows a consolidated gross profit margin of 39.5% for Q1 2022, slightly down from 40.5% in Q1 2021. Proprietary Products first quarter gross profit margin of 43.4% was 290 basis points lower than the margin achieved in the first quarter of 2021. The decline in Proprietary Products gross profit margin was caused by several factors, including lower levels of absorption during the early part of the quarter due to short-term labor constraints, increases in raw material and overhead costs. In addition, our 2021 gross profit margin included approximately 150 basis points of benefit in the prior year associated with one-time fees from COVID and other supply agreements, which did not reoccur in the first quarter of 2022. These fees had approximately 160 basis points of benefit on Q1 2021 operating margin. Contract manufacturing first quarter gross profit margin of 20.1% was 440 basis points above the margin achieved in the first quarter of 2021. The increase in margin is largely attributed to pass-through of inflationary costs and components in the quarter.

Now let's look at our balance sheet and review how we've done in terms of generating more cash for the business. On slide 11, we have listed some key cash flow metrics. Operating cash flow was \$151.2 million for the first quarter of 2022, an increase of \$62.5 million: compared to the same period last year, 70.5% increase. Our operating cash flow in the period benefited from our working capital performance. Our first quarter 2022 year-to-date capital spending was \$65.8 million, \$11.1 million higher than the same period last year. Working capital of approximately \$1.1 billion at March 31, 2022, decreased slightly by \$42.2 million from December 31, 2021, primarily due to the net reduction of our cash, offset by an increase in inventory levels. Our cash balance at March 31 of \$667.7 million was \$94.9 million lower than our December 2021 balance. The decrease in cash is primarily due to our share repurchase program and higher CapEx, offset by our strong operating results in the period.

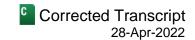
Turning to guidance, slide 12 provides a high level summary. We are reaffirming our full year 2022 net sales guidance. We expect net sales to be in a range of \$3.05 billion to \$3.075 billion. There is an estimated FX headwind of \$115 million based on current foreign exchange rates compared to a prior estimated headwind of \$70 million. We expect organic sales growth to be in a range of 11% to 12% compared to our prior guidance of approximately 10%. We expect our full year 2022 adjusted diluted EPS guidance to be in a range of \$9.30 to \$9.45, compared to a prior range of \$9.20 to \$9.35. This revised guidance includes our first quarter \$0.12 EPS positive impact of tax benefits from stock-based compensation. Also, our CapEx guidance remains at \$380 million for the year.

There are some key elements I want to bring your attention to as you review our guidance. Estimated FX headwind on EPS has an increased impact of approximately \$0.38 based on current foreign currency exchange rates compared to a prior estimated headwind of \$0.21. And our guidance excludes future tax benefits from stock-based compensation.

So to summarize the key takeaways for the first quarter, strong top-line growth in Proprietary, growth in operating profit, growth in adjusted diluted EPS, and growth in operating cash flow, delivering in line with our pillars of Execute, Innovate, and Grow.

I'd now like to turn the call back over to Eric.

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Eric Mark Green

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

Thank you, Bernard. To summarize on slide 13, our execution in Q1 has positioned us well for the year ahead. We continue to have a strong base business despite the current macro environment in which we operate. We remain well positioned with the right market-led strategy around Execute, Innovate, and Grow. We have a robust book of committed orders with momentum in 2022 and continuing into 2023. We continue to realize the benefits of a global operating model and [ph] will (17:21) continue to accelerate capital spending across our operations to meet current and anticipated future growth. With great pride, we realize the criticality of our products for healthcare across the globe, which is why our purpose to improve patient lives propels us each and every day.

Debbie, we're ready to take questions. Thank you.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Our first question comes from Larry Solow of CJS Securities. Please proceed.

Larry S. Solow

Analyst, CJS Securities, Inc.

Great. Good morning, guys. Did you give the – real quick housekeeping questions. Did you give the COVID-related sales number? Did I miss that?

Bernard J. Birkett

Senior Vice President & Chief Financial Officer, West Pharmaceutical Services, Inc.

We didn't call it out, but it was approximately \$110 million, which shows growth over Q1 2021.

Larry S. Solow

Analyst, CJS Securities, Inc.

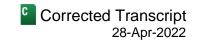
Got it. So there's no change to this year's outlook for that, it sounds like. Okay. First question, just on the cost side, clearly everybody is facing this – varying degrees of – from inflation and supply chain issues. And you guys have done a fabulous job offsetting a lot of them, I think. But obviously you only – can only offset so much. I'm just curious, with the surcharges you put in today, weren't you already kind of – is this just sort of expediting increases to keep up with the rapid – to the [ph] fluid (19:04) situation with the costs coming up? I know, normally I think you have, like kickers in there in your – a lot of your contracts. Is this more of a broader base, more aggressive reaction to some of these inflationary issues?

Quintin John Lai

 ${\it Vice President-Corporate Development, Strategy and Investor Relations, West Pharmaceutical Services, Inc.}$

Yeah. Larry, there's two elements. You're right on the contract manufacturing side of our business, which is a little bit less than 20%. We do have – with our agreements with our customers, we are passing on inflationary costs: for the most part was raw materials and et cetera. On the Proprietary side, that's more of a recent phenomena. There's two elements of that though. One is, we've mentioned before that we are revisiting our pricing strategy, and we started executing upon that last year, building up for this year. So we're seeing the element of more long-term pricing strategy around value capture that is now coming into the equation.

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In addition to that, in the Proprietary business, we have implemented surcharges as well, and that typically is really around transportation and increase in raw materials. So, there's two levers that have occurred. But I just want to be very clear that there is an element – underlying base price increase strategy is now being rolled into the ongoing business.

Larry S. Solow

Analyst, CJS Securities, Inc.

Okay. And was this kind of just enacted the beginning of this year, I guess? And I assume there's some kind of a lag, right? And margins were down a little bit. I know, year-over-year there was some more – you had this one-time – \$4 million one-time payment. I know that skewed the margins. But even if we look sequentially, margins are down a little bit, right. Is that mostly a function of these higher costs? And maybe you can't offset all of them, but hopefully maybe you get a little improvement as we look out as you enact some of these surcharges.

Bernard J. Birkett

Senior Vice President & Chief Financial Officer, West Pharmaceutical Services, Inc.

It's partly related to the cost and the lag in passing them on. So it's not always instantaneous in the quarter when you see the pricing – or the cost increases. And we work with our customers to layer that in over time, and that's what we have been doing. And the other thing that we kind of called out, Larry as well, we did see some lower levels of absorption in the – probably the first half of the quarter based on labor supply in one of our – two of our plants. And that was a short-term blip. And we've seen the absorption levels get back to normal or where we would expect them to be in the latter half of the quarter. But again, that does impact margin in the short-term.

Larry S. Solow

Analyst, CJS Securities, Inc.

Right. Yeah. That was – so my next question was, other than the cost impact and the labor issue – you call that as sort of temporary – are you guys having any major or increasing problems just retaining labor or supply chain issues, or you've been able to sort of – even though things are not getting any better, I know.

Eric Mark Green

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

I wouldn't think there is increasing problems with retaining labor. It has been challenging, I think, for everybody, but we haven't seen any spike in that. So we have a number of initiatives with our HR teams to make sure we have the labor in the right places. So, it wasn't really around a retention problem. So that's – long-term, that's not a big issue for us. And then if you look at the implied guidance, we are forecasting operating margin expansion, and to do that we have to be able to do gross margin expansion at the same time to feed into it. So, we believe some of these short-term impacts we saw at the early part of the year are kind of now behind us.

Larry S. Solow

Analyst, CJS Securities, Inc.

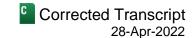
Okay. Okay, great. And then just last question on – just on back to the COVID, any – obviously there's a lot of quickly changing situation, but it sounds like for you guys – again, we've talked about it. It's not a matter of overall volume, but sort of that shift in lifecycle management. Have you seen any incremental evidence that this is occurring, or any thoughts, any update on that front?

Eric Mark Green

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

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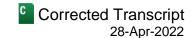


What we can share with you is that we are seeing the – more of the forecasting, looking later in the 2022, of a shift from a larger vial configuration to a smaller vial configuration. But that isn't flowing into our operations as we speak today. But that's more forecasted working with our customers in – throughout the year.

Larry S. Solow Analyst, CJS Securities, Inc.	Q
Right, right. Okay. Okay, great. Thanks, guys. I appreciate it.	
Eric Mark Green President, Chief Executive Officer & Director, West Pharmaceutical Services, Inc.	A
Thank you.	
Operator: Thank you. Our next question comes from Justin Lin of William Blair. Please pr	oceed.
Justin Lin Analyst, William Blair	Q
Hi. Good morning. Thank you for taking my questions. I guess, you know, Repligen came of yesterday and saw COVID vaccine cancellations and orders as we push to 2023 – at least them. I guess what are you seeing in your order books? And if you could share your outloo short-term and long-term, that will be great.	some of it – some of
Eric Mark Green President, Chief Executive Officer & Director, West Pharmaceutical Services, Inc.	A
Well, it's two ways look at it. One is, if we think about for 2022, our order – our confirmed of balance of the year, as we mentioned earlier, it's a very – it's much stronger than it was the year. But if you split that out, the COVID ratio within that larger order book is relatively the strelatively steady, as it was last year. Really, the expansion of that order book is really heaver also due to – over half of it's due to the success of various drug launches in our biologics space are some COVID-19 customers that are adjusting their forecast, but overall, we're see throughout the balance of the year.	e same time period last same as it – is y around the HVP and pace. So, you know
Justin Lin Analyst, William Blair	Q
Got it. So you – you're currently not sort of changing your outlook for 2023 it sounds like	
Eric Mark Green President, Chief Executive Officer & Director, West Pharmaceutical Services, Inc.	A
No we're not.	
Justin Lin Analyst, William Blair	Q
Okay.	
Eric Mark Green	^

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

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We're not, based on what we – current conversations with customers.

Justin Lin

Analyst, William Blair

Got it. And I think your margins both, you know gross and operating came slightly below the Street. You know, can you help us think through how much of that is product mix versus currency versus supply chain headwinds? You know, I think gross profit is a bit lower than you're used to seeing, but some of that is offset by lower SG&A spend as well.

Bernard J. Birkett

Senior Vice President & Chief Financial Officer, West Pharmaceutical Services, Inc.

Yeah. So, on the gross margin, really what I called out earlier in response to Larry's question, part of that was on the lower levels of absorption that we did see in the first half of the quarter. Again, that that was more of a one-time event. And what we're actually seeing in operating margin, if you look at our business on a normalized basis, if you back off the one-time take-or-pay that we got in Q1 2021 and compared operating results excluding that, operating margin would have expanded by about 130 basis points. So that – it had 160 basis point impact on operating margin. So, you know that – so when we look out for the balance of the year, we, you know, are forecasting continued operating margin expansion. So, that comp made it very, very difficult to expand the margin in the period.

Justin Lin

Analyst, William Blair

Got it. That's it for me. Thank you very much.

Eric Mark Green

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

Thank you.

Operator: Thank you. Our next question comes from Paul Knight of KeyBanc. Please proceed.

Paul Richard Knight

Analyst, KeyBanc Capital Markets, Inc.

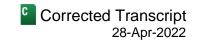
Hi. Eric, your \$380 million of CapEx obviously shows, you know, I guess a very strong building book for Biologics ex-COVID. Can you talk about 42% of Biologics – of sales or Biologics this year, what was it last year? And can you talk about what you're seeing that's driving your CapEx levels?

Eric Mark Green

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

Yeah. So we look at it, Paul, it's less than 40%. And we're seeing the Biologics become a larger piece of the – obviously it's the largest unit today, but with the highest growth, even ex-COVID in the equation. And so you think about our investments that we're currently making, a lot of the capital – over 70% of the capital is really growth-orientated, which I think historically was probably closer to the 50th percentage. And it's really focused around NovaPure and FluroTec, particularly plungers and stoppers. And what we're seeing is really a buildup. As we talked earlier about the capital that we're spending in the last couple of years really is – was already built in our five-year plan and we're just bringing it forward to support the COVID vaccines. But now what we're seeing is that the demand on the Biologics continues to increase and accelerate. And I mentioned a little bit earlier, but just to

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reiterate, I mean, if I look at the details of the [ph] confirm (29:01) order book, over half of it is of drug molecules in-market that we're seeing a ramp-up or acceleration of adoption. And so – and it's not just one molecule, it's many. So we're seeing that the pull effect of increasing volume out of West [indiscernible] (29:19) support those – the continuation of the drug in the supply chain. So we're very – very excited to see the focus around Biologics, the high penetration of successes of new BLAs or NMEs, and our participation is – remains very, very high. And this is the impact that we're seeing.

Paul Richard Knight

Analyst, KeyBanc Capital Markets, Inc.

And regarding the Corning JV, what's – I know you've indicated CapEx of \$50 million, but what's the multiyear kind of timeline in your view with that JV?

Eric Mark Green

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

Well, the investments are more in the next couple years. And I mean, it's a very long-term arrangement and we'll have various launches over the next couple years, starting this year, in 2022 of new solutions to customers. But these investments will take place on the capital side over the next couple years to increase capacity, particularly around pre-filled syringe.

Bernard J. Birkett

Senior Vice President & Chief Financial Officer, West Pharmaceutical Services, Inc.

Yeah. So that's going to be a number – a number of years before we see, from a revenue and profitability perspective. You know, that's not immediate, so it's going to take time to build that out. But in the interim, there are other configurations that we're putting together, but [ph] they won't be already (30:43) material on our numbers in the short-term.

Paul Richard Knight

Analyst, KeyBanc Capital Markets, Inc.

Okay. Thank you.

Operator: Thank you. Our next question comes from Jacob Johnson of Stephens. Please proceed.

Jacob Johnson

Analyst, Stephens, Inc.

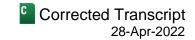
Hey, thanks. Good morning. Maybe first, just a couple of clarifying questions. First, just on the COVID side, if I heard you correctly, it sounds like your expectations for 2022 on the revenues there are unchanged. But has the composition of those revenues changed? Are you assuming – it sounds like maybe the back half of the year, you're going to get maybe a little more of a benefit from a configuration change? Is it fair to say that maybe the composition of those revenues have shifted versus prior expectations?

Eric Mark Green

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

No, I think it's pretty consistent. I think what we're seeing is, absolutely when you do lifecycle management, different bio configuration, there will be a change. And that was really more towards the back half of the year. But when we look at the growth orientation of where we are today and look at balance of 2022, the ex-COVID or the non-COVID related growth, it will outpace the COVID growth. And as you recall, last year and the year before was

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a really quick acceleration because of our response to the market. But it's more steady – if I say steady state, it's more of a lower end but still growth overall for West. But the higher element of growth in Proprietory is definitely going to come from – right now, our view is non-COVID related.

Jacob Johnson *Analyst, Stephens, Inc.*

Q

Okay. Got it. Thanks for that, Eric. And then Bernard, just on the decline in gross margin sequentially, it sounds like this was largely related to labor and absorption. And if I heard you correct, it sounds like that was the first half of the quarter and that's been resolved. So, is it fair to assume that we should see gross margins kind of bounce back, now that that's over with as we think 2Q and beyond?

Bernard J. Birkett

Senior Vice President & Chief Financial Officer, West Pharmaceutical Services, Inc.

Yeah. That's – and that's implied in the guidance that that – for that to happen. And we're confident that will take place. And as Eric has alluded, we're continuing to see very strong growth within Biologics and that mix shift within our business, and that drives a lot of that margin improvement. And we're also picking up various levels of efficiencies throughout our operations. So we would expect to see margins continue to improve throughout the year.

Jacob Johnson

Q

Analyst, Stephens, Inc.

Okay. That's helpful. And then just last question, kind of getting to the point I think you both want to make. You know, Eric, you mentioned a long horizon of organic growth. I guess the question there, what would be helpful – just remind us kind of where High Value Product units stand in terms of percentage of units today, you know what that number looks like and maybe how that could – what that could look like, maybe five years from now.

Eric Mark Green

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

Yeah. If you think about the algorithm that we have with the – greater than 70% of our sales in Proprietary is High Value Products. The units – number of units that we are producing for High Value Products is roughly around 22%, 23%. And the way it works is about a 100 basis point expansion on units is strong double-digit growth on High Value Products. If you think about how Biologics is becoming a larger portion of the portfolio – again across many different customers, so it's not really concentrated on one customer or one drug: it's across the whole portfolio of the market. That will continuously drive higher revenues, higher profits with not a lot of increase on units per se, a 100, 100-plus basis points. So that's the equation. And we expect that to continue. It's the fastest growing sub-segment with the injectable medicine space. The pipeline is very robust. It was very encouraging to see the number of new approvals over the last 12, 18 months in this particular space, and our participation rate is high as ever. So, all this equates to – and it translates into our [ph] confirm (35:21) order book for future launches. So, this all translates into continued growth for the next five years of HVP for West.

Jacob Johnson

Analyst, Stephens, Inc.

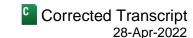
Perfect. I'll leave it there. Thanks for taking the questions.

Eric Mark Green

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

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Thank you.
Operator: Thank you. Our next question comes from Derik de Bruin of Bank of America. Please proceed.

Derik de Bruin Analyst, BofA Securities

Hi. Good morning, everyone.

Good morning, Derik.

Eric Mark Green

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

Derik de Bruin

Analyst, BofA Securities

So, my apologies if I'm going to repeat some stuff, but can you just sort of talk about the organic revenue growth guide? You're a little bit below in our numbers in the first quarter, yet you raise it for - 1% to 2% for the full year [indiscernible] (36:07), which is surprising given the Q1. Can you just sort of walk through me – can you just sort of walk through the math on your confidence in sort of getting that increase given the good start.

Bernard J. Birkett

Senior Vice President & Chief Financial Officer, West Pharmaceutical Services, Inc.

Yeah. So the – when we look at it – and it goes back to the point I made earlier about the absorption rates that we experienced in the first half of the year due to some of our labor constraints, and that was primarily around Omicron. It impacted us in [indiscernible] (36:35) in a couple of different sites. Again, that was a short-term problem. That impacts our ability to produce in the short-term, so then that kind of leads into some impact on our revenues in the first quarter. So it's not that we're seeing a drop or a shift in our demand downwards: it's mainly what we could actually produce in the quarter and deliver to customers. So, that was a little bit light. But as Eric said, our order book is still very, very strong and we also had – when we had spoke earlier on in the year, we were saying we were going to see more of our growth come in the back half of the year versus the first, and that's still what we're seeing. So, there is really no change.

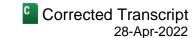
Derik de Bruin Analyst, BofA Securities

Great. Thanks for clarifying that. That's really helpful. I didn't get to that. Have you - I've got a couple of clients asking, can you just sort of confirm that you're looking for greater than 100 basis points of overall operating margin expansion this year?

Bernard J. Birkett Senior Vice President & Chief Financial Officer, West Pharmaceutical Services, Inc.

Yeah. And again, that's implied in the guidance. So, it will be greater than 100 basis points. And just back to the point I made earlier, if you look at the fundamentals of the business, that if you take that take-or-pay that we had in Q1 2021, if you back that out and then look at the comp on that basis, operating margin would have expanded about 130 basis points. So, from a comm point of view, you had that level of challenge here in the first quarter. So when I look at that, it gives me confidence to be able to say, yeah, we are going to continue to expand that operating margin.

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Derik de Bruin

Analyst, BofA Securities

Do you think the production constraints are largely [ph] alleviated (38:23) now?

Eric Mark Green

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

I'll comment. I would say, just based on the last couple months' performance, I would say, yes. I mean, there's always challenges in this environment today. The couple plants that Bernard is referring to, we were hit hard on the Omicron and that did impact absorption: it also impacted on productivity. But over the last couple months, looking at the productivity levels, the output, we do believe we have very good control around this. And we are able to build/flex to make sure that we're able to deliver going forward. But it was a short-term hit.

Bernard J. Birkett

Senior Vice President & Chief Financial Officer, West Pharmaceutical Services, Inc.

Yeah. So, we did see improvement as we moved through the quarter. And we are forecasting that to continue based on what's in place now.

Derik de Bruin

Analyst, BofA Securities

Great. And I've got some people asking on your China exposure and just sort of any commentary in that region: has that been a headwind to the business at all?

Eric Mark Green

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

Yeah. So, our operations was impacted in the sense that our Qingpu manufacturing facility is within the region of Shanghai, and obviously our offices too. So we did have a site closure for a short period of time, and we're working through that now. As far as materiality for West, it's very low percentage for West coming out of that facility for the local market. But we're keeping an eye on it, make sure that we can pivot and potentially import where necessary versus having materials coming out of that specific site. We do expect to see a recovery in this quarter with the demand, but we need to stay tuned because that's kind of a dynamic environment right now.

Derik de Bruin

Analyst, BofA Securities

Great. Thank you very much.

Eric Mark Green

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

Thank you.

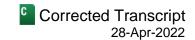
Operator: Thank you. Our next question comes from Dave Windley of Jefferies.

David Windley

Analyst, Jefferies LLC

Hi. Good morning. Thanks for taking my questions. I just want to follow up on Derik and some of the other questions – the line of questioning around the capacity. Wondering if your absorption commentary on productivity

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issues affected your ability to deliver to clients? Like, should we think about, revenue would have been higher in the quarter if you had been able to produce as much as you expected in those facilities, and like did the lag times to clients change at all?

Bernard J. Birkett

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Senior Vice President & Chief Financial Officer, West Pharmaceutical Services, Inc.

Yeah, it impacted it slightly, but it didn't really impact lead times overall. You know, we were able to kind of get that product out to customers, you know, in the early part of this quarter. So, there was – you know, we tried to minimize any customer impact. As we said, it happened earlier in the quarter, but there is no, kind of long-term impact to that. It was a once off and it was something we've been able to deal with, and we've been able to continue supply to our customers. You know it did – could impact revenues slightly, but not overly material, I will put it that way. But there was some – there was some impact around that.

David Windley

Analyst, Jefferies LLC

Okay. On the – it seems as people have already highlighted, the gross margin impact and somewhat offset by SG&A being a little lower. Should we think about that SG&A level as durable? Is that a result of kind of some permanent productivity step-ups?

Bernard J. Birkett

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Senior Vice President & Chief Financial Officer, West Pharmaceutical Services, Inc.

Yeah. It is durable. It's productivity – and again it's looking at what is the appropriate level for SG&A of our business. And that's something that we manage very, very tightly.

David Windley



Analyst, Jefferies LLC

Okay. And then a somewhat longer term question around capacity. I apologize I'm probably not great at keeping up with all this, but you've pulled forward quite a bit of CapEx not just kind of now but over the COVID period and have a number of initiatives in place to bring more capacity online. Could you just help us understand in broad strokes, when those capacity expansions are supposed to hit – and I think it's mostly FluroTec and NovaPure as you've highlighted, Eric – and then also confirm that – confirm what you said in the past that you basically expect that capacity to be taken up by order demand right away. In other words, no dilution to productivity, absorption, et cetera, as you're bringing on slugs of new capacity. Thanks.

Eric Mark Green

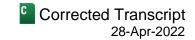
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President, Chief Executive Officer & Director, West Pharmaceutical Services, Inc.

Yeah. I'll start with the last part first and say that we don't anticipate any impact if there's variability around the COVID piece, because if we look – again, look at our – the demand that we're getting with non-COVID related, particularly in the Biologics space, which is – overlaps 100% with the investments that we are putting in, the growth is actually – is a little bit higher than we anticipated. So, therefore, we're in a position we can absorb that. But to your first point, the initial launch that we communicated back in – early on in the pandemic, let's call it 2020, that investment is now finalized and in place and now through, is producing commercial product this year. And it was kind of weaved in throughout 2021. So that's 100% installed.

The second phase that we communicated really towards the early part of 2021, we're seeing that being layered in as we speak and might leak some parts of it – not all, a portion, small portion might go into 2023, but the focus of the remaining HVP is exactly you stated: it's really focused around NovaPure and FluroTec capacity and it is

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across multiple plants within our network. And again, it lines up very nicely with the growth in Biologics and it also does support pharma and generics but mostly Biologics. And then growth in Biologics in our order book is extremely strong as we speak today.

So I'm pretty confident. Now, we need to get that equipment in, installed, validated. And we've been doing a great job across the globe. We also need to add some resources to be able to run those – the new equipment. And that is ongoing as we speak. So we're seeing a very good uptick on attracting new -additional talent to our organization, but also doing a good job of keeping in pace with the capital expansion.

David Windley

Analyst, Jefferies LLC

Excellent. I appreciate those answers. Thank you.

Eric Mark Green

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

Yeah. Thank you.

Operator: Thank you. I would now like to turn the conference back to Quintin Lai for further remarks.

Quintin John Lai

Vice President-Corporate Development, Strategy and Investor Relations, West Pharmaceutical Services, Inc.

Thanks, Debbie. Thank you for joining us on today's conference call. An online archive of the broadcast will be available on our website at westpharma.com in the Investor section. Additionally, you may access a replay through Thursday, May the 5th by using the dial-in numbers and conference ID provided at the end of today's earnings release. That concludes this call. Have a nice day.

Operator: This concludes today's conference call. Thank you for participating and you may now disconnect.

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