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West Pharmaceutical Services, Inc. (WST)

Bank of America Merrill Lynch Health Care Conference

CORPORATE PARTICIPANTS

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

MANAGEMENT DISCUSSION SECTION

Derik de Bruin

Analyst, Bank of America Merrill Lynch

[ph] Good evening (00:00:02), everyone. Welcome to the 2018 Bank of America, Merrill Lynch Healthcare Conference. I'm Derik de Bruin, the Life Sciences and Diagnostics Tools Analyst, CROs, CDMOs and Animal Health. Thank you for being here. Remember, it's [ph] II (00:00:18) season, so we appreciate your support because I'm shameless.

Anyhow, our next company is West Pharmaceutical Services. With us today is Bill Federici, CFO. Bill's got some opening slides and then we're going to open it up to fireside chat and Q&A. With that, Bill, thank you for being here. Always a pleasure.

William J. Federici

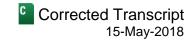
Chief Financial Officer & Senior Vice President, West Pharmaceutical Services, Inc.

Thank you. Well, thank you, Derik. And thank you, Bank of America, for allowing us to be here today to present the story of West Pharmaceutical Services. I'll point you to our Safe Harbor statement which provides you the information about management's discussion of forward-looking statements. You can see our website for more full details.

So West is a 95-year-old global manufacturing company that really grew up understanding and are experts in how drugs and materials interact. We are the leading global manufacturer of components and systems for injectable drug medicines. As you see on this slide, we work with everybody. We are of the top 50 injectable biologics. They rely on West or our Japanese affiliate, Daikyo, for their primary drug components and systems. We are a top 75 producer for all of the major biotechs and pharmaceutical companies. In fact, we work with all of the major biologic, pharmaceutical, generic and medical device companies in the world.

The interesting thing about West or one of the many interesting things about West is we manufacture 41 billion things annually, about 32 billion on our proprietary device side and the rest is in our contract manufacturing side. We're going to talk about it over the course of these presentations but there's three moats around this business that make it quite a – it's not unique, but a very differentiated business. We have a regulatory moat around the business that is everything that we do that's the primary drug container is specked into the drug master file for that drug when it gets approved. And we are on the life of the drug unless someone were to want to redo all the stability work to change this out which really doesn't happen.

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The second moat around the business is our capital moat. We've deployed \$1.7 billion in our 28 global manufacturing facilities that produce these 41 billion things a year, so quite an amazing amount of productive capacity for our customers' important injectable medicines. And the third one is the industry itself, which is slow to change. And that slowness to change impedes a lot of new entrants into the marketplace.

So I mentioned it's a great business. It is truly over the last five years, as you can see on the slide here, in terms of our constant currency growth rate of about 6.4% over that five-year time horizon, our EPS grew on a constant currency basis, on an adjusted diluted EPS basis of about 14%. And you can see there off to the right, the TSR chart for the stock over the last five years has been exceptional as well.

We are — I mentioned, work with everyone. One of the great things that Eric Green when he took over as CEO about three years ago did was he turned the company from being a products company into a company that addresses the market by market unit and all of the unique needs of those markets. So whether it's the generics companies who have a need for speed and quality, or the pharma markets who are looking for the best, most effective total cost of ownership of their injectable drug meds, we work with all of them and their very specific needs. And it's actually helped us to become better adept at changing from being a products company to more market demand, more market need.

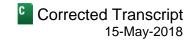
And this is really the height of what West does. West is a company that, as we said, provides these very special primary drug containment and delivery systems for injectable medicines, and it starts all the way from us providing very simple, straightforward, molded and trimmed product that we ship to a customer. That customer then would have to wash and sterilize that product before it can be injected into the human body. That's a standard product. That's what you see at the lower left-hand corner of your screen.

Those sell for about \$0.01 to \$0.02 a piece. All the way up from there, we have expanding our increasing value to West, but also our increasing intimacy with the customer in terms of high-value products from categories from where we do the washing which is a process we call Westar where we have also FluroTec coated stoppers that work very well with our biologic customer drugs. Envision systems where we look at every single component that's being manufactured. We take – we do camera inspections to look for defects so that we can give the customer the most – the highest quality, best product with the lowest particulate levels. All the way into some of our delivery systems whether they be Daikyo's Crystal Zenith solution or our SmartDose. And from an elastomer perspective, all the way up through NovaPure which is our quality by design product where up there we're selling things for \$1 or more per unit versus the \$0.01 to \$0.02 for a standard stopper.

And this is really crux of the growth story of West. If you think about it, off to the right hand side of the screen you see this is a chart of both the five-year sales CAGR and the gross margin associated with these product categories. Our high value product components, those are those things from Westar up that curve that we showed is growing. As you can see here on the chart, north of 10% a year over the last five years and its margins is about twice that of the standard packaging product which is growing about zero to low-single digits and the margin is less than 30%. If you think about this, the five-year CAGR for the company on a sales basis is again that 6.4% on an annual basis.

One of the things that West does, in addition to manufacturing at a very, very high level on such a grand scale, is the 41 billion components that we manufacture, components and devices. As we provide these customers with the scientific expertise and the technical customer service to be able to support their products through the development phase and into their commercialization phase. We work very, very closely with the customers from very early stages in their development of their product all the way from the either pre-clinical or early phase clinical products where we get involved in helping the client understand what are the attributes of that particular

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drug product, and what are the things that they need to do from a packaging perspective to be able to keep that drug safe and effective during its entire life cycle that is sitting on the shelf, whether it be in the supply chain, at a doctor's office or in the patient's refrigerator. Those are the things that we work on and are experts in and help us continue to innovate and be innovative to our customers.

Speaking of innovation, we spend about 2.5% of our sales on an annual basis on research and development activities. Mostly D, we don't do a whole lot of R, but a lot of D, especially around the components that we manufacture and the delivery systems that our customers use and the administration systems that they use to get the drug product into the body. These are truly innovative things that we're working on. We're known to be innovative in the industry. And as it says there on the slides, these new product introductions that have been introduced over the last five years have provided more than a 100 basis points of organic sales growth in 2017, so not only a robust R&D pipeline but also one that's very productive for West.

I mentioned our 28 manufacturing facilities manufacturing 41 billion things a year. Over the last 95 years we've been truly innovative in manufacturing as well. We manufacture – if you take that 41 billion, over 110 million components are manufactured on a daily basis in these 28 facilities. And the remarkable thing about it is our standard of quality that we achieve through our manufacturing process and our quality standards. We're able to not only talk about being able to beat Six Sigma, but we beat it by a mile. We are talking about our out of spec products in the parts per billion not parts per million. So quite an accomplishment.

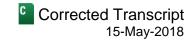
We also have a contract manufacturing business in addition to providing our own proprietary products. We have customers who prefer to own the intellectual property of their products and have West do the complex engineering design, automation and commercialization and industrialization of those products for them. We've been doing that for the last 50 years. The majority of our contract manufacturing skills came to us in the acquisition of the Tech Group in 2005. It says there we produce 8 billion components for delivery systems for our customers on an annual basis, and it is across eight manufacturing facilities across the globe. So again, a very, very robust contract manufacturing business. That is a very big strategic plus for West. This is where our global footprint for the manufacturing network for all of our plants around the globe.

From a global operations perspective, we just completed the construction and validation process of our Waterford, Ireland site. We started the construction back in 2014. We are literally now just finishing up all of the validation protocols on that, on the first phase of that, which will be to provide risk mitigation services for our customers, sheeting material for the cartridges that go into insulin pens. So a very important product that we manufacture here in Waterford, Ireland that will start commercial sales in the back half of 2018.

For the first quarter, we reported those results as of – on April 26, and you can see the slide that we presented at that point in time. We reported that as basically flat sales growth, but talked about the headwinds that were associated with that sales growth of both Venezuela deconsolidation and the loss of a product from a consumer-product customer, contract-manufacturing customer, that without those things, our growth would've been about 4.1%. Our adjusted diluted EPS was \$0.62 and we had some tax benefits associated with that as well. We looked at our – reaffirming our 2018 guidance at that point in time of \$1.72 billion to \$1.73 billion at \$1.20 per €1, and a constant currency growth rate of 68% associated with those sales and adjusted EPS of \$2.80 to \$2.90 at that \$1.20 per €1.

The most important thing, though, is this long-term financial construct. We talked about the beauty of the business, the moats around the business and how important the business is to our customers, very important injectable drug products. Well, we believe that we can continue to grow as we have over the last five and even last 10 years, that 6% to 8% range for a very, very long time on an organic basis. It's based upon the principle of

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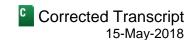
not only selling the – being involved in the customers' new drugs that are being brought to market, but also helping the customer in those very important ways to address their regulatory or other market needs in terms of bringing cleaner product to the marketplace. And the way you do that is you sell more incremental value by downstream processing of those products and selling them devices associated with those products. That's the way we get to the 6% to 8% organic sales growth.

Along with that, you'll have 1% price increase, you'll have 2% to 3% market volume increases, and 3% to 4% of that mix shift that's selling more and more value per product sold. We believe in association with that, there's a very high correlation between those high-value product growth that we talked about and margin expansion. We believe that we can expand operating margins by 100 basis points on average in any given year based on that construct. And we believe our annual capital expenditures will be able to be maintained within \$150 million to \$175 million range. That, coupled with our expanding operating cash flows, allows us to continue to believe strongly in our ability to continue to grow free cash flow over the time periods going forward.

So in summary, it's really a lot about building for the future. This is a company that has got a very, very strong history of being a critical component manufacturer for the injectable drug space, one whose criticality is evidenced every year and in the high penetration rates that we have in the various market segments that we have focused on. Our competitive position from not only our strong cultural values but also our ability to continue to work scientifically and with our customers to make a better product, one that's cleaner, one that operates better, and one that helps keep their drugs safe and effective while in the supply chain.

We have a global operations footprint that produces a tremendous amount of volume at very, very high quality to our product, to our customers. It's at the core of what we do every day. And we have financial strength to invest. We're completely de-levered on a net debt to total invested capital basis. And we continue to see that our growing strong operating cash flow will be enough to help us along with our existing debt structures to be able to help us to continue to grow into the future.

So I thank you, Derik, and I'm happy to take some of your questions.



QUESTION AND ANSWER SECTION

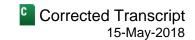
Derik de Bruin Analyst, Bank of America Merrill Lynch	Q
Great. Thanks, Bill. So just to clarify, your organic revenue growth guidance this year is 6% to 8%, and that coming off of basically 0% in the first quarter. Are you off of that – are you doing the 6% to 8% off of the 4% adjusted or off the 0%?	
William J. Federici Chief Financial Officer & Senior Vice President, West Pharmaceutical Services, Inc.	A
We're doing it off of the 0%. So it's a constant currency base. Now, if you take t numbers, you're going to be at the low end of that 6% range. If you take them of that range.	
Derik de Bruin Analyst, Bank of America Merrill Lynch	Q
Okay. That's good news. But it still doesn't imply a significant ramp up in the ba	ick half?
William J. Federici Chief Financial Officer & Senior Vice President, West Pharmaceutical Services, Inc. It does. It does.	A
Derik de Bruin Analyst, Bank of America Merrill Lynch The second quarter guidance was still lower?	Q
William J. Federici Chief Financial Officer & Senior Vice President, West Pharmaceutical Services, Inc.	A

Second quarter we'll see a moderation. So we'll see a better flow of product, better sales score for us in the second quarter, but marginally so and then certainly being able to be helped in the back half of the year by a number of things. First one is as we get out of the first quarter, there's no more Venezuela impact that goes away. We deconsolidated Venezuela as of April 1, 2017, so therefore it is no longer in our numbers. It no longer creates a headwind.

We also talked about the fact that we have some more easier comps coming forward. First quarter 2017 was a real strong quarter for us. So the comps get a little easier as we go into the back part of the year. We're seeing strong demand for our products, not only from the generic side of the business, but also from Pharma as well and from contract manufacturing. So those things, coupled with a shortage in the bags that are used for infusion, we have a product that helps connect the vial to those bags that's in short supply or the demand outstrips our supply.

So we have new capacity that's coming on in the third quarter that we believe will be – it's a product that works with all different kinds of bags. So it's a universal bag connector and it will be a very good strong grower for us in the back half of the year which will help Pharma out as well. So we put all of those things together. We believe that we're getting much closer to our customers in terms of understanding their supply situation and their demand

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situation, getting a little more transparency into the supply chain so we can actually start to work with those customers, not only to help us level load our plants, but also look to them to help them reduce their working capital loads. They don't have to keep as much advanced stock, as much working capital if we can provide them with a product that they get a shorter lead time. Well, if they can provide us with their true demand, not just what they think for the next 60, 90, 120 days but what their real demand is and what they're seeing in the supply chain in the channel down from them, we can do a better job of helping use our levers in our own manufacturing capacity to level-load our plants and provide them with a shorter lead time.

Our lead times have come down, and Derik, you know we had expanding lead times in the 2016 timeframe into 2017's due to some issues with customers from both the regulatory and a upgrading perspective that we did some Lean manufacturing concepts on our own shops and we were able to introduce Kinston as an additional washing facility for Westar that expanded the capacity and brought down those lead times back into more of a normal lead time. So we are now able with much more confidence to be able to address the customers' demand needs in terms of their cycle times for ordering through delivery. And that gives them confidence to be able to give us more exposure into their supply chain. So it's a win-win for both sides. So all of these things, when we put them all together, gives us a good amount of comfort. We are not going to – we're going to grow marginally in the second quarter, but the back half of the year we feel very good about.

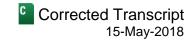
Derik de Bruin Analyst, Bank of America Merrill Lynch	Q
Got it. And are you still targeting 100 basis points of margin expansion this year given the – because it was - first quarter was a little low.	
William J. Federici Chief Financial Officer & Senior Vice President, West Pharmaceutical Services, Inc.	A
Yeah. So let me go into that.	
Derik de Bruin Analyst, Bank of America Merrill Lynch	Q
The hole, yeah. Yeah.	
William J. Federici Chief Financial Officer & Senior Vice President, West Pharmaceutical Services, Inc.	A

Yeah, we dug ourselves the hole from the headwinds associated with that. We won't get there on a basis if you include all of the headwinds in there. But when you strip out Venezuela and some of the contract manufacturing customer and some of the overhead underabsorption associated with some of our newer facilities, then we will get to the 100 basis points for the full year. And more importantly, as we look out into the future, Derik, based on the constructs which we hadn't lost any business, we still believe fundamentally in our ability to continue to grow high-value products in that high-single digits to low-double digits that we have in the past. And we believe we'll be able to continue to expand margins from that perspective. So we feel very comfortable about the long-term construct not changing and our ability to do that into the future. This year is particularly difficult based on the beginning of the year.

Derik de Bruin

Analyst, Bank of America Merrill Lynch

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So the – I think one of the questions we've had, as you add sort of new capacity to it and just sort of given the historical, I would say, choppy visibility, what's your confidence that you can sort of fill all the capacity that's coming online over the next couple of years?

William J. Federici

Α

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

We will not fill all the capacity over the next couple of years. We've talked about Waterford is starting from a zero right now, right?

Derik de Bruin

Analyst, Bank of America Merrill Lynch

Yeah.

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

And we're just literally – I mean, we're producing validated product today but commercially sellable product will happen starting in the third quarter. So that facility is going to take a long time, several, several years to fill up that capacity. Kinston, North Carolina, we added capacity there for things like NovaPure and for additional Westar washing capacity, that's only about 30% to 40% penetrated at this point in time in terms of utilization. So that's also got room to grow as well.

So the good news is that when you think about all of the costs associated with those activities, it's already being borne by the company. So each additional unit that's processed through there will have a nice margin impact for us. So we believe very good – very, very confident in our ability to continue to grow based on all the things we've talked about. But you're right, those two facilities in particular, as well as some others, will take years before they are completely utilized.

Derik de Bruin

Analyst, Bank of America Merrill Lynch

So the high-value products have gone from 34% in 2012, 41% in 2017. Sort of walk us through where that is the next five years.

William J. Federici

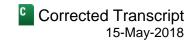
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Chief Financial Officer & Senior Vice President, West Pharmaceutical Services, Inc.

Sure. So what we've talked about is if you look at it on a number of units bases which is a little bit easier way of looking at it, [audio gap] (00:24:28-00:24:38) are still standard products. On average, we believe that that will grow about 100 basis points a year. And when we looked at it in 2016 at the end of 2016, it was around 17% or so. It's about 18.5% at the end of 2017. So it works, that view of it may be growing about 100 basis points.

But when you step back and you look at the composition of the high value products, it's really a bunch – it's a portfolio of high value products. The oldest ones, the ones that have been around for the longest amount of time are Westar and FluroTec. They were both introduced in the late 1990s, early 2000s and they still have room to grow. Not all of the things we produce today use either Westar or FluroTec. So there's still ability to grow. Remember what I said earlier is every single one of these primary drug containers, the components that comes in contact with the drug, has to be washed and sterilized. So someone needs to do that. We are doing it on average about 40% of the time. So there's room to grow there.

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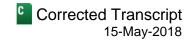


FluroTec, the same thing, that's used as a stable, impermeable barrier between the drug and the packaging materials. That's used a lot in the biologics context. That still has room to grow. Things like Envision, our camera inspection systems, those things are less than 10% penetrated. Less than 10% of the things that we use, that we manufacture today have that. Think about it. If you're able to produce a product and reject the quality issues, things that are out of spec or there's some kind of [ph] contaminant (00:26:31) associated with that product, before you fill the product at the end of the customers' filling line where they put the API into the container, you save them a lot of money by being able to reject it before it gets the drug inside of it. So there's an economic compulsion for doing that. That's less than 10% penetrated today so that has a huge amount of runway associated with it.

And then NovaPure and things like SmartDose and CZ, these are very nascent technologies, less than 1% penetrated at this point in time. And while they're not nearly as – the addressable market isn't nearly as huge as the entire market that we see on the component side, there's a lot of room for growth in all of those high-valued products. So it gives us a lot of comfort that we should be able to continue to grow our high-value product components on average in the high-singles to low double-digits like we have. If you look at it over the last five years and over the last 10 years, last five years it was about 10.5% growth in high-value products on an annual basis. Last 10 years is just over 10% as well. So those are things that give us comfort that we will continue to grow into the future.

Derik de Bruin Analyst, Bank of America Merrill Lynch	Q
And I mean, talk about your plans. I mean, you're retiring?	
William J. Federici Chief Financial Officer & Senior Vice President, West Pharmaceutical Services, Inc.	A
Sure.	
Derik de Bruin Analyst, Bank of America Merrill Lynch	Q
And so how's the search for a replacement going?	
William J. Federici Chief Financial Officer & Senior Vice President, West Pharmaceutical Services, Inc.	A
Thank you. Yeah, it's going well. It's a search that is ongoing at this point in time. We've had a lot of int position, which is good. I think that's healthy. And we're committed to an orderly transition process here soon as we have something to announce we'll be out there to announce it.	
Derik de Bruin Analyst, Bank of America Merrill Lynch	Q
And I guess – a question [indiscernible] (00:28:18).	
	Q
I just wondered [indiscernible] (00:28:20) growth, how should you look at your growth prospects geogra Asia?	aphically in

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William J. Federici

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

Sure. So Asia has been growing very well for us, it's one way to imagine. The question was how should we think about growth in Asia going forward. In the first quarter, we're seeing strong double-digit growth in all of our Asian markets and I expect that that will continue. Obviously, those markets are growing faster than the Western markets. Anyway, ours is a smaller business where not even 10% of our market is in Asia but we certainly think of that as a very strong area for growth for West in the future.

Derik de Bruin

Analyst, Bank of America Merrill Lynch

So we're coming down the end, my standard question, what's underappreciated, what's misunderstood about West?

William J. Federici

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

I'll tell you this is one of those great businesses that has a tremendous, long stayed history of being able to be a key partner to the injectable drug industry, whether it be in terms of developing the quality products that allow the drugs to be able to be safe and effective in their primary drug container for the shelf life of the drug. We also have a tremendous amount of scientific capacity and capabilities where we help the customer not only in the early-stage development of their drugs, but in terms of how those drugs then any regulatory questions or things that they have that they experienced in the gestation of their drugs through the development pipeline.

The third thing is from a manufacturing capacity, we are a very special company. We have a lot of plants. We have capacity to produce things, many, many billions of things in a high-quality repeatable basis. We look at it and we talk about our quality culture. We believe very, very strongly in not only our ability to manufacture at a high-quality basis, but in that it's the right thing to do. And we look very, very carefully at what we do on an annual basis but also on a daily basis. We may produce 41 billion things, but every one of those components has a patient's name on it and that's the way our people, all 7,500 of them, go to work every day.

William J. Federici

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

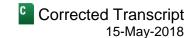
So thank you very much.

Derik de Bruin

Analyst, Bank of America Merrill Lynch

Thank you very much.

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