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# West Pharmaceutical Services, Inc. (WST)

Stephens Investment Conference

## CORPORATE PARTICIPANTS

### Quintin John Lai

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

### Chad R. Winters

*Chief Accounting Officer, Vice President & Controller, West Pharmaceutical Services, Inc.*

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## OTHER PARTICIPANTS

### Jacob Johnson

*Analyst, Stephens, Inc.*

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## MANAGEMENT DISCUSSION SECTION

### Jacob Johnson

*Analyst, Stephens, Inc.*

All right. Good afternoon, everybody. Welcome to the final session of Nashville 2022. We're going to end with a good one. I'm Jacob Johnson, the life science tools and pharma services analyst here at Stephens. Really pleased to be joined with the team from West this afternoon. We have the man of many hats, Quintin Lai, VP of Corporate Development, Strategy and Investor Relations; and then, Chad Winters, VP and Controller. So, fireside chat format. I'll run the Q&A, but try to open up to the audience here.

And with that out of the way, Quintin, I'll turn it over to you for any opening remarks and then launch in the Q&A.

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### Quintin John Lai

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

Well, thank you. And on behalf of West, Chad and I would like to thank you, Jacob and your associates, for hosting us here at this conference. It really well-run the conference and we've had a very good day of meetings. So, thank you again.

So, for those of you who may be not as familiar with West, I'll just give you a quick rundown. We are a global leader in primary packaging of and delivery of injectable drugs. We manufacture stoppers, plungers, seals. We do wearable devices. We do contract manufacturing where we're making injection molding components used in diagnostic devices, injection devices. We have 25 sites around the world. And we have been on this journey for the last 100 years, powered mainly by the growth of the injectable drugs industry and, in particular, over the last few years by the biologic injectable drug industry, so.

## QUESTION AND ANSWER SECTION

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

All right. Perfect. So, appreciate the high-level comments which means, inevitably, I'm going to turn to some of the near-term dynamics. But I promise, we'll come back to longer-term opportunities.

So, just maybe with that as a jumping off point, third quarter results, a bit lighter than we and I think you likely expected. Maybe that as a starting point, just talk about headwinds and what drove the shortfall in the quarter?

**Quintin John Lai**

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

A

Sure. So, as we were entering into Q3, as expected, COVID-19 sales started to decline year-on-year. And then, with that expected decline, we knew that we had capacity that we would then be able to dedicate to processing products that have had really long lead times because, through the pandemic, we had been prioritizing components used for COVID-19 vaccines, which meant that lead times from some of our other products lengthened. And in some cases orders, that customers placed for 2022 delivery were being pushed out to 2023. So, as that capacity freed up, we were able to bring in some of those orders. Now, when we do so, they're not as productive. I mean, it's our base business, which means multiple SKUs for multiple customers compared to COVID-19 products where a fewer SKUs and higher runs. So, there's just a productivity mismatch.

What we expected though was that we expected to be adding capacity, especially at some – at a couple of our North American high-value product manufacturing sites. And as the quarter progressed, we hit some project delays which meant that we were unable to get that incremental capacity online. So, even though our non-COVID base business grew in the quarter, it didn't grow as much as we had anticipated.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Yeah. So, I think you called out equipment downtime as maybe a \$30 million revenue headwind in 3Q. As we think about your guidance for the year and what it implies for 4Q, is there any way to frame up how much of a headwind there is in 4Q from it?

**Quintin John Lai**

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

A

Yeah. So, by not being able to bring on that additional capacity, Jacob, we were – we estimated it was about a \$30 million shortfall in Q3. So, when we reframed guidance for the year, what we assumed is that the issues that we had in Q3 would be resolved by early 2023, so that means that, Q4, we'll have a full quarter.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Yeah.

**Quintin John Lai**

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

A

So, you can take that \$30 million which impacted us in September and kind of bring it across the full Q4.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Okay, got it. And then just in terms of your guidance assumes it comes online in early 2023. But I'd assume, you're working harder to get it done sometime before then. Any thoughts around that?

**Quintin John Lai**

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

A

So, the teams are working through those issues. The equipment, especially the equipment that we are talking about, it is in place, it is being installed. We are going through the processes. We have informed customers who have to go through their own validation process. So, again, we feel good about the timeline that we set and we look forward to updating you as we continue to make progress.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Got it. So, this seems to be a supply issue, not a demand issue. But I think investors are probably concerned around the near-term demand environment. So, maybe, no shortage of things people are worried about. But why wouldn't stocking biotech funding kind of impact demand for your high-value products?

**Chad R. Winters**

*Chief Accounting Officer, Vice President & Controller, West Pharmaceutical Services, Inc.*

A

Yeah. I mean, I think first, if I start with the biotech funding, right, that happens at such an early stage in the process from a drug development perspective, and we're really more influenced by commercialized products. But from a stocking perspective, this is something that we discuss with our customers frequently. We're monitoring buying patterns or monitoring orders, so we're not seeing any anomalies right now associated with that. But it is something that we are constantly keeping an eye on.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Yeah. Thanks for that, Chad. I mean, just the sheer number of SKUs you have mean that it's probably less likely that you're seeing stocking and maybe if you are seeing it anywhere beyond the COVID side of anywhere?

**Chad R. Winters**

*Chief Accounting Officer, Vice President & Controller, West Pharmaceutical Services, Inc.*

A

We certainly – yeah, I should have clarified that.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Yeah.

**Chad R. Winters**

*Chief Accounting Officer, Vice President & Controller, West Pharmaceutical Services, Inc.*

A

You're absolutely right. On the COVID side, there continues to be volatility...

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Yeah.

Q

**Chad R. Winters**

*Chief Accounting Officer, Vice President & Controller, West Pharmaceutical Services, Inc.*

...and there likely is some destocking going on there. I mean, the volume of SKUs certainly could contribute to that [indiscernible] (00:06:50).

A

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Okay. And then, just to get COVID out of the way, \$90 million of COVID revenue in 2023, how much benefit does that assume from lower dose per vials? And maybe any updates – updated thoughts on lower dose per vials?

Q

**Quintin John Lai**

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

So, over the period, we've already been supplying components of different sizes for different vial configurations. So, really, as we were formulating that is our preliminary guidance for 2023, it's based on what our order book looks like now as well as conversations that we're having with our customers. And so, that's what's driving it and, I think, less about the how much is going into multi-dose versus single-dose and more how many doses just in general are being ordered.

A

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Okay. Yeah. Got it. That makes sense. So, you did give some frameworks around kind of the 2023 revenue outlook, but there's one piece you didn't give too much disclosure on which is the outlook for margins next year. And that's the number one question investors have, and Quintin's smiling at me because he knows this one's coming. So, if we use 4Q as a jumping off point, it would seem to imply gross margins in the low-to-mid-30s. Can you just talk about how much of a drag there is from the lack of equipment? And do you have certain lines where you're essentially bearing 100% of the cuts but not generating any revenue?

Q

**Quintin John Lai**

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

So, let's kind of look at the fourth quarter...

A

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Yeah.

Q

**Quintin John Lai**

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

...and let's look at what we're seeing right now is that we anticipate COVID sales to decline approximately \$80 million year-on-year.

A

**Jacob Johnson***Analyst, Stephens, Inc.*

Q

Yeah.

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

A

We're going to – based on our October guidance, we see FX headwinds.

**Jacob Johnson***Analyst, Stephens, Inc.*

Q

Yeah.

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

A

We don't anticipate any change in the inflationary trends that we've seen throughout the entire year. On the other side where we have been giving some pricing and so, in the first half of the year, it was around 3.4%, 3.5%. In Q3, it was about 4.4%, and so probably similar amount in Q4. And then, what we've assumed is that no incremental volume coming in from new capacity. And so, what it means is that what we're missing is that ability to bring on that incremental HVP sales and which would also help given the fact that with our overhead absorption. So, although you've got three headwinds – FX, COVID, inflation – no change in the pricing and no incremental. And that's kind of what drives both the gross and operating margins that is implied with our guidance.

**Jacob Johnson***Analyst, Stephens, Inc.*

Q

Okay. And then, the other thing you alluded to earlier was this productivity gain around COVID because you are making a lot of the same component over and over again. Is there any way to – you had really impressive margin expansion the last couple years. Some of that, certainly, was from base business growth, which was strong, but there's also the COVID piece of it and that had to have some productivity gains. Is there any way to frame up how much of the margin expansion the last couple of years was from productivity gains?

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

A

Yes. Good question. So, the core business, the base business over the last few years has grown in excess of our financial construct. And if you look at the components of driving that, they were HVP sales. It was NovaPure and FluroTec in our Biologics business. It was Westar and, in some cases, NovaPure in our Generics and Pharma business. And so, given the makeup of that drivers of the base business over the last three years, we believe and we estimate that we would have exceeded that financial construct of 100 bps of operating margin expansion per year.

Now, that said, COVID sales were also layered on top and they have an even higher percentage of HVP sales compared to our base proprietary products business, which makes them even more profitable and brings even more incremental sales growth. So, the answer is that the expansion that you've seen over the last couple years, it was both. And so, yeah, we just break it out like that.

**Jacob Johnson***Analyst, Stephens, Inc.*

Q

Yeah. Okay. Well, I'll try one last one and then, I promise, we'll move off this topic. But \$90 million of COVID next year, that's not dissimilar to 2020. I have a feeling I know the answer to this. But any reason why that's not – it may be a fair comparison of how people should be thinking about margin next year in proprietary products?

**Quintin John Lai**

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

A

Yeah. So, we haven't given guidance to 2023. But on your hypothetical – yeah, I guess, if you could tell me is your hypothetical also that costs are going to be like 2020? Right?

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Yeah.

**Quintin John Lai**

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

A

So, how about this, let's look at it this way. Next year, what we see is that we expect a drop in COVID sales. So, going from probably approximately \$280 million October sales, and we've already said they are more profitable than our base business. We didn't guide to FX because we only gave organic sales growth guidance. What we said is that we anticipate at least growth, so that implies that at least low-teens in proprietary. That assumes that we're bringing on new capacity online, especially all the issues that we had.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Yeah.

**Quintin John Lai**

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

A

But we didn't give you what the number could be. We're, right now, working through our issues and, when we give our guidance, we'll be able to have that for you. So, that – there's potential upside to that. And then, on the other side is the pricing. We never did – you know what we've done for pricing so far here in 2022. And what we said on the call is that we're in the process of informing customers of our 2023 pricing and, again, that is a TBD as well.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Okay. Last margin question and I promise this time. Just in terms of there's been no shortage of inflationary pressures this year, I think freight costs, energy costs, labor costs come to mind. Can you just talk about how those have trended throughout this year and any thoughts about that into next year?

**Chad R. Winters**

*Chief Accounting Officer, Vice President & Controller, West Pharmaceutical Services, Inc.*

A

Yeah. I mean, I think you hit the right ones right?

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Yeah.

**Chad R. Winters**

*Chief Accounting Officer, Vice President & Controller, West Pharmaceutical Services, Inc.*

A

Freight, labor, raw materials, energy costs, no doubt that's been a headwind all year. Yeah, that's been factored into our Q4. What we said last month for the fourth quarter, but again it's too close – tough to call right now for 2023. That's also factoring into those pricing discussions, obviously, with the customers are being very transparent...

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Yeah.

**Chad R. Winters**

*Chief Accounting Officer, Vice President & Controller, West Pharmaceutical Services, Inc.*

A

...in having this discussion as well.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Would it be fair to say that energy, labor, probably still some pressures there? We cover a bunch of transportation companies here. It sounds like freight costs may be that's cooling off a little bit right now. Is that fair? Are you guys still seeing pressures from that?

**Chad R. Winters**

*Chief Accounting Officer, Vice President & Controller, West Pharmaceutical Services, Inc.*

A

I think we're still seeing some pressures there, yes.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Yeah, okay. All right. Okay. Let's kind of think longer-term or more interesting things. Just within high-value products, let's place that COVID aside because that was also a lot of FluroTec, NovaPure. Can you just talk about the mix shift you've seen within high-value products in kind of the base business as it relates to FluroTec and NovaPure in recent years?

**Quintin John Lai**

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

A

Sure. So, when we look at mix shift, there are two major drivers there. One is pipeline drugs. So, drugs that have been approved over the last few years, predominantly, are Biologics. And since we've launched NovaPure, many of them have adopted NovaPure. And as those drugs have gained traction, expanded their indication, entered into new geographies, the volumes are growing and that has been powering our sales from the mix. So, really it's more the – not necessarily a conversion of FluroTec to NovaPure, it's just adoption of NovaPure over FluroTec because FluroTec used to be the premium product a decade ago. Now, it's NovaPure.

On the other side, it's legacy customers and those legacy customers that were, perhaps in the past, buying standard product from us and washing and sterilizing themselves for a variety of reasons. They have decided to move up and adopt our Westar process, which means that we will then wash and sterilize, and there is a meaningful jump in ASP. So, the volumes are still the same; it's just that, now, we are selling HVP process. And then, there is another subcategory of customers that were already buying one level of HVP and perhaps moving



to, let's say, a vision-inspected product which would also give an ASP boost. And so, both had been successful for us here and we anticipate will continue to be so here over the next few years.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Okay. I think something, I think, most who are familiar with the story understand but, I think, it's important piece of it is high-value products, meaningful portion of revenue; but in terms of units, low-20s still. How much runway is there for – in that journey from a unit perspective?

**Quintin John Lai**

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

A

So, as we look at it, you're right, Jacob. I mean, in terms of penetration of HVP, in terms of our overall, it's still modest. If you look over the last few years, it's been growing about 100 bps of volume improvement every year. And we think that we still have continued runway for that for the next few years. And again, it's going to be a combination of conversion of legacy. That's a modest number. But what we're seeing is that customers only move up in quality, they don't move down. And then, second is pipeline. And the pipeline drugs that are coming out now, they're almost all starting at the HVP level. And so, as they launch and have successful expansions, again, that also will then drive the number of HVP components.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Got it. And then, just kind of focusing again on FluroTec, NovaPure as we think about ex-COVID growth next year, you have COVID rolling off which I think is a lot of FluroTec, NovaPure, but where are you adding capacity, well, it's FluroTec, NovaPure. I think Eric mentioned maybe NovaPure Plungers is a key area of growth next year. Can you just talk about kind of ex-COVID demand for – within high-value products, where are you seeing the most strength there?

**Quintin John Lai**

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

A

So, in the short-term which is the what impact us in the third quarter, that was more just HVP processing.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Okay.

**Quintin John Lai**

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

A

But we also have expansion projects that are going on now at all of our HVP sites, both adding equipment in existing facilities as well as building expansions or brownfield expansions, if you will. And some of those brownfield expansions are going to be for dedicated NovaPure capacity. And what we're seeing is that there is growing demand, especially on the plunger side, which would suggest an increase in demand in the prefilled syringe market.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Yeah. We'll get to maybe some of the demand drivers behind that. But maybe first, we'll take a little bit of a detour and just talk about the journey you're on on high-value products. You talked about FluroTec being the previous kind of high-value product, and then NovaPure came along. You've got this interesting partnership with Corning. Can you just talk about the strategy behind that relationship, what the value proposition will be for customers? And then, timeline and financial perspective, what would it look like?

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**Quintin John Lai**

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

**A**

So, if you look at, at the journey from FluroTec to NovaPure, what there is you see the importance of quality by design and how customers value that concept, value the improved quality, reliability that comes with packaging their precious drugs. And you can see how they've embraced that. And it's because not only do they get better reliability, they get better yield, but it also fits the regulatory environment because the regulatory environment is pushing for a QBD type of principles as well.

The similar thing we think is happening on drug device combination of products. We see it firsthand when we've developed our wearable technology, the requirements that the regulators put our customers and us through to show robust performance for putting a drug in a dedicated device. They're taking a look now at, okay, taking some of that drug device combination therapy and how can that work as for components that are, right now, fragmented for glass elastomer, the fill finish, and brought together and called the system; but they're really not truly a system because it's a separate Drug Master Files for each component.

So, the opportunity we have with Corning is that we're working with an established glass supplier, tremendous technology and skill set and resources that they have. They have ability to supply both borosilicate glass as well as aluminosilicate glass which has superior properties in many ways to borosilicate glass. We will be – we're investing with them. We're investing in manufacturing. They are going to be making product for us. And the goal will be a designed, integrated system, glass elastomer that will live under a single Drug Master File. It'll be the industry's first truly integrated system and one that no longer be fragmented. And we think that it will bring value to the customer, both in terms of quality reliability, potential yield, as well as fit within the framework that the regulators are setting for things to work together as a system.

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**Jacob Johnson**

*Analyst, Stephens, Inc.*

**Q**

And as we think about that, is that something you could convert existing customers to? Or should we think about that as something kind of for new launches that's more of an opportunity?

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**Quintin John Lai**

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

**A**

I think that that given the – how our industry works, understanding that we do work in a high-inertia business where change is not easy for people who've already adopted products. It will probably follow what we – our NovaPure experience, which is that drugs that are in the pipeline and, as they go through their different clinical phases, we'll then start to spec in. And then, when they get approved, that's when we'll start to see the first adoption.

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**Jacob Johnson**

*Analyst, Stephens, Inc.*

**Q**

Okay. And just remind me the timeline for kind of when that gets commercialized, what that looks like?

**Quintin John Lai**

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

We haven't said.

A

**Jacob Johnson**

*Analyst, Stephens, Inc.*

[indiscernible] (00:24:20)

Q

**Quintin John Lai**

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

It's just we are in the process we announced this year. We're investing in facilities, pilot facilities. We're doing the development work. And so, we'll keep you updated as we continue to make progress.

A

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Oh, okay. Got it. And then, there's delivery devices which, I think, are a little bit different than how we think about high-value products, but you could argue that they're super high-value products. Can you just talk about what SmartDose and SelfDose are for those who are less familiar?

Q

**Quintin John Lai**

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

Sure.

A

**Jacob Johnson**

*Analyst, Stephens, Inc.*

[ph] I have some follow-ups (00:24:51).

Q

**Quintin John Lai**

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

So, we'll start with SelfDose. SelfDose is our design for an autoinjector. It is a patient-powered autoinjector. Unlike the autoinjectors most of you are familiar with, those are spring loaded; this one is something that you can place on the body and with the palm of your hand push and apply, press the plunger to have it injected into the body. It's great for people for drugs that are being delivered – self-delivered by patients who might have dexterity issues. And so, we see it as a niche product that fits applications for that category.

A

SmartDose is a wearable device that you can – that can range from 3.5 milliliters up to 10 milliliters. The concept is that you can take a drug that would – you can formulate down just easily to a prefilled syringe or an autoinjector and instead fill it into that device that'd be user-filled. The patient would put it – place it on their body, push a button. And then, over a period of time, whether it be minutes, whether it be hours, depending on what the drug customer decides, it can deliver that dose into the body. And the real advantage here is being able to take drugs that are currently infused in a clinic or in a hospital. Take that IV bag drug, reformulate it down to, say, 10cc's, and then be able to have the customer be able to apply it at home. So, it is a trend that, I think, has just only accelerated since the pandemic with now an understanding that patients really do prefer the ability to be able to self-administer as opposed to having to – have to drive in and go see a clinic every three weeks.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Yeah. So, if I'm not mistaken, I didn't get this still confusing. I think SmartDose just received its fourth approval? Okay, I got a nod.

**Quintin John Lai**

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

A

That's right.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

I got that right. Just that last point you made, I think it makes a ton of sense and we probably haven't talked a ton of SmartDose and SelfDose over the last couple years because there is COVID to talk about. But that trend, the healthcare movement in home is pretty powerful. Like if we look out the next couple years, do you think these become kind of a bigger piece of your business if the world is moving that way?

**Quintin John Lai**

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

A

So, it's one of those things where, you're right, we don't talk about it very often on the calls, but the interest level continues to grow higher and higher. And it's not just from new drugs but it's from existing drugs that are reformulating and moving from IV to subcu. And so, yeah, you're right, we've had three approvals this year and we have a very good pipeline of candidates that are looking to move to SmartDose.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Got it. And then, maybe it probably relates more to SelfDose than SmartDose, but I'm curious kind of your thoughts here, Quintin, which is it seems to me some pharma companies have developed their own pens, their own delivery devices. Is the target customer for SmartDose and SelfDose kind of mid-sized biopharma or is the offering more differentiated than that? Just kind of curious, your thoughts there.

**Quintin John Lai**

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

A

Yeah. So, good question. So, for SmartDose, no, it is for some of the largest companies as well as some of the smallest company. So, because the SmartDose wearable infuser is the only one out there, it's gotten attraction from a variety of customers. In the case of autoinjectors, yeah, autoinjectors is a little different there. There comes – yeah, sometimes companies have their own design and, in that case, we'll work with them on the contract manufacturing side. Sometimes, they don't have their design and they're looking for something unique, and there's where our SelfDose product provides something that, again, it's not for everyone but it is a differentiated product that does fit a niche.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Okay. And then, as it relates to kind of customer pens that they developed, you mentioned contract manufacturing, maybe it's an opportunity on that side of the business. For the people who manufacture those pens, is there any – are you selling proprietary product components to them for that at all?

**Quintin John Lai**

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

A

So, if it's an autoinjector or a pen, most likely inside, there's going to be a cartridge. And if there's a cartridge, there's going to be a plunger. And on the other end of the cartridge, if it's a reusable autoinjector where you're putting needles in and out of it, there's going to be a multi-laminate seal on the end and we would participate in both of those.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Okay. All right. So, then, as we think about end markets and key growth drivers, maybe a couple just to run through. Diabetes and weight loss drugs and neuro drugs seem to be where there's some interest from investors. Can you just talk about those end markets as potential opportunities for West?

**Quintin John Lai**

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

A

Yeah. We don't go down that path. But what we said is that it is an exciting time to be a supplier in the injectable medicines market.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Okay.

**Quintin John Lai**

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

A

And because of that and because of the enthusiasm of some of our customers that they're seeing, we have not slowed down our capital projects. So, even though we are seeing or expect to see a drop in COVID-19 sales in 2023, we are moving forward with our capital expansion plans and we've got capital expansion projects at all five of our sites going on right now.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Okay. And then, maybe just last kind of end market question. Biosimilars, those are coming next year and probably will continue to come after that. Can you just talk about maybe the level of high-value product a biosimilar may use versus the originator given the originator was developed years ago when NovaPure didn't exist?

A

So, the name says it all. It is similar to the innovator drug which means it's a macromolecule, which means it's going to have all the frailties that the innovator drug has to the drug packaging, whether it be extractable [indiscernible] (00:32:17), whether it be silicone oil, whether it be whatever that comes along with it. And so, with it, at a minimum there, we'll use the HPP packaging most likely that the innovator use. But what we're seeing in some cases is that they are looking to move up toward NovaPure and in some cases they're even looking for even better than what we have with NovaPure. And so, it just kind of underscores that, just because it's a biosimilar, they actually have higher concerns of improving quality.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Got it. Maybe, I'll pause there to see if anybody in the room has any questions. If not, I've got a couple more. Go ahead. I'll rephrase.

Q

[indiscernible] (00:33:04-00:33:31)

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

For those listening, the question is, can you take 2019 margin and, if you're assuming COVID goes away, can you add 100 bps a year? And should that be what 2022 looks like? And maybe, Quintin just talked about the ex-COVID growth over the last couple years and maybe what – I'm not sure you could tell us what that number would be ex-COVID, but why [ph] it probably was (00:33:55) maybe more than 100 bps over the last couple years?

**Quintin John Lai**

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

A

No, thank you for the question. So, the way to look at it is so, perhaps, we can use Q4 as an instructive way to look at it. Our implied guidance for the fourth quarter of this year is for EBIT margins to be a shade under 20%, all right. Compare that to what 16% that you had in 2019. And what do we see in Q4? We see large COVID headwinds. We see FX. We see inflation with some offset in price and no incremental capacity coming online that brings in incremental HVP sales. So, what we anticipate is that we're going to be bringing on that incremental HVP capacity next year. And we think that that EBIT margin that we implied in Q4 is not a number that we would move forward with. It should be better than that.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

All right. We've talked a lot of proprietary products, just contract manufacturing. Can you just talk about the factors that weighed on growth in 2022? And then, you're, I think, pointing to that return into growth in 2023, just how much visibility you have into that?

**Chad R. Winters**

*Chief Accounting Officer, Vice President & Controller, West Pharmaceutical Services, Inc.*

A

Yeah. I'll give Quintin's voice a break.

**Jacob Johnson**

*Analyst, Stephens, Inc.*

Q

Thank you, Chad.

**Chad R. Winters**

*Chief Accounting Officer, Vice President & Controller, West Pharmaceutical Services, Inc.*

A

Yeah. So, as you rightly said, right, 2022, we saw a slight decline. We had visibility to that, right, so that was in our guidance at the beginning of the year. There wasn't a surprise. As we said on the call in October, return to growth, that's probably that low-single-digit growth. But the same visibility that the transparency of our customers,

working with our customers that we have at the beginning of 2022 we're heading into 2023 with that same visibility based on our production schedule with customers.

**Jacob Johnson***Analyst, Stephens, Inc.*

Q

And, Chad, is that a business that just inherently kind of can shift around year-to-year? I know that proprietary products is more of the story and the key growth driver. But is that a business, given the nature of it being outsourced, that there's only so much you can control what it's going to look like in a given year?

**Chad R. Winters***Chief Accounting Officer, Vice President & Controller, West Pharmaceutical Services, Inc.*

A

Well, I mean, sure. I mean, if you look back in 2022, right, we had a customer that decided to move some of those volumes to a different supplier, so that's obviously out of our control. So, that's certainly a dynamic that can happen.

**Jacob Johnson***Analyst, Stephens, Inc.*

Q

Okay. Then, maybe, capital allocation. Quintin, let's start with something you mentioned. One of the recent questions is you're still going forward with capacity expansions. Traditionally, maybe CapEx has been a little more modest. But given the growth you've seen the last couple of years has been kind of through an investment cycle, how should we think about that kind of duration of this CapEx investment, kind of stepped up CapEx investments you've made the last couple years? Or Chad?

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

A

So, the way we look at it is, looking out on the long horizon and our financial construct of 7% to 9% top line and 100 bps of margin expansion per year. In that type of environment, we think 6% to 7% of sales for CapEx should be the appropriate manner of reinvestment to support that top line growth. Now, everything comes with an asterisk. And when there is indications of upside demand for that, then we have to build ahead. We are in a business where capacity addition is something that takes 12 to 18 months to get in place. And so, because of that, we have to build ahead of the curve in order to make sure that we can meet the customer expectations.

**Jacob Johnson***Analyst, Stephens, Inc.*

Q

Got it. And then, maybe last question for me, just on capital allocation. I think since Eric came on board, very focused on organic efforts and you guys have done a great – a phenomenal job there. But you have mentioned the potential for M&A over the last year or so. You've done some interesting partnerships like the Corning one. But just kind of any thoughts on M&A and what could be interesting to you?

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

A

Sure. Well, you're right, Jacob. I mean, the number one focus for the capital allocation has been organic sales growth, [ph] one of which has (00:38:29) been CapEx. We're always looking for opportunities to bring more value to the industry, to patients, and really it just starts with that. M&A for us is that all about the value creation. We want to do it in such a way that we are bringing together something that's differentiated; something that, because the industry has a high inertia to change, it has to be something that is much better than whatever the incumbent



is out there. And so, the combination with us brings that synergies. And so, with that, most of what we've been doing is mostly technology licenses, sometimes equity investments. When the opportunity comes, we'll definitely take it, but that's our strategy.

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## Jacob Johnson

*Analyst, Stephens, Inc.*

Got it. All right. Well, Quintin, Chad, thank you so much for being with us in Nashville today. We really appreciate it.

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## Quintin John Lai

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

Thanks, Jacob.

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## Jacob Johnson

*Analyst, Stephens, Inc.*

Thank you.

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