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West Pharmaceutical Services, Inc. (WST)

Q1 2020 Earnings Call

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

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Analyst, Bank of America Merrill Lynch

Paul Richard Knight

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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by, and welcome to the First Quarter 2020 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. [Operator Instructions] Please be advised that today's conference is being recorded. [Operator Instructions]

It is now my pleasure to introduce Vice President of Investor Relations, Quintin Lai.

Quintin John Lai

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

Thank you, Andrew. Good morning and welcome to West's first quarter 2020 conference call. We issued our financial results this morning and the release has been posted on the Investors section on the company's website located at westpharma.com. This morning, CEO, Eric Green; and CFO, Bernard Birkett will review our results, provide an update on our business and present our updated financial outlook for the full-year 2020.

There is 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 2 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. The company's future results are influenced by many factors beyond the control of the company, and actual results could differ materially from past results as well as those expressed or implied in any forward-looking statement made here. 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's 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. Thank you for joining us today. The past several months have been some of the most difficult times for our communities across the world as we face challenging circumstances related to COVID-19. This pandemic has made clear the importance of global healthcare and the criticality of the role West plays during these unprecedented times. Our mission to improve patient lives cannot be any more meaningful than in times like today. We take great pride that for nearly 100 years we have provided innovative high quality products and solutions for the containment and delivery of injectable medicines.

Despite the COVID-19 challenges, the West team remains focused on creating and delivering value to all our stakeholders. West has two priorities that are guiding us through this pandemic. First and foremost we're focused on the well-being and safety of our team members across the globe. Our crisis management team was engaged at the outset implementing precautionary measures across our company to protect our teams. It seems nearly every day I learn about another great way that our team is stepping up to deliver the critical components to meet the urgent needs of our customers and their patients while looking out for the safety of one another. These moments are not only inspirational but they serve as a testament to the collective strength of the One West team and I'm grateful for their unwavering commitment to our mission. In addition, our culture of philanthropy and community involvement has our team members offering their time, unique skills and knowledge in support of local response efforts.

Turning to slide 4. Our second priority is the continuity of manufacturing and supply of components and solutions to our customers. The strong tenets of our market-led strategy and globalization of the manufacturing network are contributing to the resiliency of West business in today's climate. I'm pleased to say that the growth trends we experienced throughout 2019 have continued in the first quarter and the outlook for the balance of the year remains positive. Despite the current challenges, so far, we have been able to maintain our operations at normal capacity. For the benefit of our customers we have been able to leverage our world-class global manufacturing network by enabling the right capabilities, scale and flexibility to keep up the increase in demand. Because of the constantly changing environment and its effect on the economy we conduct business impact analyses daily and make adjustments as they are required. These assessments are an integral part of our business continuity plans within each of our global sites and operations network.

Throughout the past several months we have monitored our supply chain, including our close partner Daikyo, and at this time do not foresee any negative impact from direct or indirect suppliers. As the pandemic has intensified, as expected, we have seen an increase in customer orders in recent weeks. We are monitoring order flow to ensure that we are addressing the true demand for our products.

As shown on slide 5, despite today's uncertain environment, I am pleased to report that we had a strong first quarter performance and we enter the second quarter well-positioned. We had 13% organic sales growth in the first quarter, largely through strong high-value product sales. This resulted in double-digit growth in adjusted EPS for the first quarter. As we enter the second quarter, the demand for our products continues to be solid from both existing customers as well as new opportunities from companies looking to develop COVID-19 solutions. Each

day seems to bring new challenges, supply chain, transportation, government regulations, and I want to emphasize that across West, we're operating with a sense of urgency to address and manage these issues.

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

Bernard J. Birkett

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

Thank you, Eric and good morning. I hope everyone is healthy and safe during this time. Now let's review the numbers in more detail. We will first look at Q1 2020 revenues and profits where we saw strong sales and EPS growth, led by strong revenue performance primarily in our Biologics and Generics market units and contract manufacturing. I will take you through the margin growth we saw in the quarter as well as some balance sheet takeaways. and finally, we'll review guidance for 2020.

First up Q1. Our financial results are summarized on slide 6 and a reconciliation of non-US GAAP measures are described in slide 13 to 16. We recorded net sales of \$491.5 million representing organic sales growth of 12.7% and 30 basis points of inorganic growth. Proprietary Product sales grew organically by 11.8% in the quarter. High-value products, which make up more than 63% of Proprietary Product sales, grew double digits and had solid momentum across all market units throughout Q1.

Looking at the performance of the market units, the 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 high-single digit growth led by sales of Westar and FluroTec components. Our Pharma market unit saw mid-single digit growth with sales led by high-value products and service, including Westar, NovaPure and FluroTec components. And contract manufacturing had double-digit organic sales growth for the first quarter, led once again by sales of diagnostic and healthcare related injection systems.

Moving to slide 7, we continue to see improvement in gross profit. We recorded \$167 million in gross profit, \$20 million or 13.6% above Q1 of last year, and gross profit margin of 34% with a 90 basis point expansion from the same period last year.

We saw improvement in adjusted operating profit with \$88 million recorded this quarter compared to \$71.3 million in the same period last year or a 23.4% increase. Our adjusted operating profit margin of 17.9% was a 180 basis point increase from the same period last year. And finally, adjusted diluted EPS grew 36% from Q1. Excluding stock tax benefit, EPS grew by approximately 31%.

So what's driving the growth in both revenue and profit? On slide 8 we show the contributions of sales growth in the quarter. Volume and mix contributed \$51.1 million, or 11.5 percentage points of growth. Sales price increases contributed \$6.6 million or 1.5 percentage points of growth. And changes in foreign currency exchange rates reduced sales by \$9.7 million, or a reduction of 2.2 percentage points.

Looking at margin performance, slide 9 shows a consolidated gross profit margin of 34% for Q1 2020, up from 33.1% in Q1 2019. Proprietary Products first quarter gross profit margin of 40.2% was 130 basis point above the margin achieved in the first quarter of 2019. The key drivers of the continued improvement in Proprietary Product gross profit margin were a favorable mix of products sold driven by growth in high-valued products, production efficiencies and sales price increases partially offset by the increased overhead costs. Contract manufacturing first quarter gross profit margin of 14.3% was 30 basis point above the margin achieved in the first quarter of

2019. Our adjusted operating profit margin of 17.9% was a 180 basis point increase from the same period last year largely attributable to our Proprietary Products gross profit expansion.

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 10 we have listed some key cash flow metrics. Operating cash flow was \$57.1 million for the first quarter of 2020, an increase of \$9.5 million compared to the same period last year, a 20% increase. Our Q1 2020 capital spending was \$32.1 million, \$3.3 million higher than the same period last year and in line with guidance. Working capital of \$633.1 million at March 31, 2020, was \$74 million lower than at December 31, 2019, primarily due to a reduction in our cash and cash equivalents. Our cash balance of at March 31 of \$335.3 million was \$103.8 million less than our December 2019 balance primarily due to \$115 million of expenditures under our share repurchase program. Our capital and financial resources including overall liquidity remained strong.

Turning to guidance, slide 11 provides a high level summary. Full-year 2020 net sales guidance continues to be in a range of between \$1.95 billion and \$1.97 billion. This includes an estimated headwind of \$26 million based on current foreign exchange rates compared to prior guidance which forecasted a \$15 million headwind. We expect organic sales growth to be approximately 8%. We expect our full-year 2020 reported diluted EPS guidance to be in a range of \$3.52 to \$3.62 compared to prior guidance of \$3.45 to \$3.55. Capital expenditure will be in a range of \$130 million to \$140 million.

There are some key elements I want to bring your attention to as you review our guidance. Estimated FX headwind on EPS has an impact of approximately \$0.07 based on current foreign currency exchange rates compared to prior guidance of \$0.04. The revised guidance also includes a \$0.07 EPS impact from our first quarter tax benefits from stock-based compensation.

So to summarize the key takeaways for the first quarter, strong top line growth in both Proprietary and contract manufacturing, gross profit margin improvement, growth in operating profit margin, growth in adjusted diluted EPS and growth in operating and free cash flow. Our sales and EPS projections for 2020 and performance are in line with our long-term construct of approximately 6% to 8% organic sales growth and EPS expansion.

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

Eric Mark Green

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

Thank you, Bernard. Our company is financially strong. Today, more than ever, the pursuit of our mission is priority and that's taken for granted. West products are needed by patients across the globe and in many cases for the administration of lifesaving medicines. As the market leader we are committed to ensure continuity of supply to our customers around the globe. In addition, we are supporting our many customers that are developing potential solutions to address COVID-19 with components for diagnostics, anti-viral therapeutics and vaccines.

We are confident in our long-term growth strategy. Although these are trying times, we are opportunistic and dedicated to doing what is necessary supporting the healthcare industry as it works to resolve this global pandemic. We will emerge from this experience collectively stronger. And on behalf of all the team members at West, it is our wish that you stay healthy and safe in the days ahead.

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

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] And our first question comes from the line of Larry Solow with CJS Securities.

Larry S. Solow

Analyst, CJS Securities, Inc.

Q

Good morning, guys. Thanks for taking my questions and congrats on a good quarter. Good start.

Eric Mark Green

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

A

Great. Thank you, Larry.

Larry S. Solow

Analyst, CJS Securities, Inc.

Q

Just on the Proprietary sales, a question on that side of it, obviously very good growth – coming from the usual suspects here. I'm particularly impressed with the margin side on the gross side, 130 bps up year-over-year. And I think last year Q1 was also a very good quarter. So, on a full-year basis, it was up over 150 bps. Yeah, I'm not asking will these trends continue, but what – if you peel back the onion a little bit, seems like obviously mix is driving a lot of that and is that – just the mix within mix as you not only increased your high-value products percentage, but maybe go up the scale within high-value products to more of like say the NovaPure and stuff like that. Can you give us a little more color on that?

Eric Mark Green

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

A

Yeah, Larry. Good morning and thank you for the question. It's good to hear your voice. You're absolutely correct is – what's happening with Proprietary is really two levers are being pulled simultaneously. One is the high-value product mix effect but more importantly is that we're seeing increased growth and contribution of that growth with the products that have even higher margins. We started thinking about NovaPure, Daikyo Crystal Zenith, even the FluroTec. When you look at those in totality, that's roughly let's say about half the incremental growth when it comes to the high-value products and with much higher margin. So, the mix shift is occurring through high-value products but even more pronounced was the higher margin subsets of that portfolio.

The second lever that we are holding and the team is doing a really good job is this globalization of our operations. And as you know, we've been on this journey for a couple years now and the team has done a phenomenal job to start implementing lean processes and initiatives across our plants. It's allowing us to be more efficient, be more effective and higher throughput. So the combination of both of them are giving us that type of margin expansion in Proprietary, and what excites me is as we think about the future pipeline, it is around the NovaPure, the FluroTec, the CZ, the self-injection portfolio and that's what's really exciting as we think about the long-term growth trajectory of this business.

Larry S. Solow

Analyst, CJS Securities, Inc.

Q

Okay. Great. And then just switching gears [indiscernible] (00:19:22) on COVID-19, just sort of a couple of questions there, how do you gauge sort of surge in orders true – versus sort of true demand, any timing impact and the – is the gear-up in diagnostics and potential vaccines and therapies, is that even – is that moving the

needle for you guys in this short run? And then lastly on the COVID, with the drop in oil – significant drop in oil, realize there'll be some lag effect to that, but I would assume that would benefit you guys as we look out over the next few quarters? Thanks.

Eric Mark Green

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

A

Yeah. Larry, in the COVID-19, specifically around our sales and products being introduced to support, and I mentioned three areas around diagnostics, therapeutics and also vaccines, in Q1 we did not see any incremental revenue as a company due to COVID-19. We had some – frankly, Bernard can give you a little more detail but we did have some additional costs. But what we're seeing right now, and with the approach we've taken with the market units, we're able to have much more granular discussions with our customers. As we started thinking about Q2 and Q3, we are actively working in all three corridors.

To give you an example, in the diagnostics, our contract manufacturing arm of the business, is currently scaling up on consumable products that are used in the couple of the devices that are – been introduced in the market recently. We won't speak about any specific customer, but these have been introduced recently into the hospitals and the clinic setting. When it comes to therapeutics, there are a few that are in the market that we're already supporting and then commercialized, but they're currently, as you know, going through clinical tests to see the ability to combat COVID-19 and we're in those...

Larry S. Solow

Analyst, CJS Securities, Inc.

Q

Right.

Eric Mark Green

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

A

...areas. And then lastly...

Larry S. Solow

Analyst, CJS Securities, Inc.

Q

Right.

Eric Mark Green

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

A

...the vaccines. And those are a little more long term as we look out to 2021. And our FluroTec technology is perfect candidate for the vaccines market. So it's kind of a staged approach and we'll see some of the...

Larry S. Solow

Analyst, CJS Securities, Inc.

Q

Right.

Eric Mark Green

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

A

...benefit in 2020 and – but most of it'll be in 2021. Do you want to, Bernard, talk about the oil impact?

Bernard J. Birkett

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

Yeah, so the – there are some – there'll be a tailwind from oil, but there's also some headwinds that we're going to see to offset that. So particularly around the logistics side and on freight, we're seeing some increased costs there given the well-documented issues of getting products to customers and just the supply chain itself, and the impact COVID is having on that. And then we have all – we have also some other costs that we're absorbing in supporting our employees as we're managing through the pandemic. We saw some of it in Q1 and there were some – primarily showed up in our CM gross margin, which was probably impacted most by that. But I think, again, we will see some benefit but there are other headwinds and offsets there.

Larry S. Solow

Analyst, CJS Securities, Inc.

Got it. Okay. Great. Thank you, guys. Appreciate it.

Eric Mark Green

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

Okay. Thank you, Larry.

Operator: Thank you. And our next question comes from the line of Paul Knight with Janney.

Paul Richard Knight

Analyst, Janney Montgomery Scott LLC

Hi, Eric. Could you talk about what you need to do to minimize the risk of a facility shutdown? I know you're operating in a – effectively a cleanroom operation in many sites, but do you have to go another step higher? Do you do alternate shifts? What do you do to reduce your risk for these facilities?

Eric Mark Green

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

That's – thank you, Paul, and good morning. No, you're absolutely correct. We took a very proactive approach months ago when we've started to see what we learned from our colleagues in Asia, particularly in our Qingpu facility in China and also in Singapore. What we've done is we've taken a – there's multiple steps that we've taken. One is we've split shifts to minimize – as they do the shift handovers, minimize interaction and so that social distancing is very important, also temperature monitoring. We also put a program in place that only essential employees were allowed to go into the facilities. So you can imagine at our plants, of the 25 plants throughout the world we have very important roles but these are individuals that they actually can work from remotely, and we put that in place immediately.

One other element we put in place is we really focused on ensuring that when our colleagues are not feeling well or there's some question about their health, that they don't feel pressure to come into the office. So we relaxed some of our attendance policies. We improved – we expanded our compensation if somebody had to stay home for a period of time [ph] then that's (24:40) covered, taking care of themselves and/or their family members. So those are many different levers that we put in place, and to ensure that people that are in the plants, should be in the plants and also mitigating any risk that we have from maybe coming from the outside.

This crisis management team we put in place is monitoring this daily. We can tell you [ph] any of those absenteeism (00:25:05) issues in any particular site, and I am very pleased and actually humbled on how well the

absenteeism is very low in multiple – at multiple sites and I know in Europe it went up slightly but it came back down to normal rates in the last several weeks which is a real testament our employees really understand the purpose or why we're doing this and to support the community. So there's a lot of levers that we pulled Paul, it's not just one solution, there are many and we're not going to let off on the intensity of our processes. We cannot afford to have an issue at a plant.

Paul Richard Knight*Analyst, Janney Montgomery Scott LLC*

And lastly, regarding – can you tell if there was stocking going on in the industry in Q1?

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

Yeah, Paul we did not see stocking. I'll tell you why, our business very well is that we're really made to order. So, November and December is really the time period of when we look at Q1 demand that we need to manufacture over the following three to four months. I will tell you this though, in the recent weeks, the conversations have intensified where customers are coming to us and that's where our commercial organization has done a great job of categorizing and working with customers to alleviate their concerns, not to do increase in safety stock because our lead times have not increased because of the global network that we've put in place. So, we were able to categorize any incremental revenues is it due to vaccines, therapeutics, supporting therapies, hospital enablement, and also, frankly, increase in safety stocks and that's what we're keeping an eye on at this point in time. That hasn't as been as pronounced. We've learned our lesson back in 2015 and 2016 and so we are very conscious of that and we have the right programs in place to monitor and manage through this.

Paul Richard Knight*Analyst, Janney Montgomery Scott LLC*

Thank you.

Operator: Thank you. Our next question comes from the line of David Windley with Jefferies.

Hi, good morning. This is [ph] Dan Lee (00:27:22), on for Dave. Thanks for taking our questions. I think you mentioned in Proprietary Products that your mix is improving toward higher margin HVPs and I wanted to just hone in on NovaPure a little bit. Can you give us a sense of how large that is as a percentage of Proprietary Products and what the growth is? And then, is the growth being driven by existing products or an expansion of the product portfolio in that line?

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

It's twofold. One is it's expanding the NovaPure or Nova brands portfolio with additional products and capabilities. But it is – if you think about Nova, NovaPure is actually close to a double on an absolute dollar value during the quarter, and that's the trend that we're currently seeing that started back in late 2018 and 2019. I'd give you an example, one new product portfolio that we had launched with the NovaPure is the one with 3mL, which we believe [indiscernible] (00:28:29) which we believe can continue to help have this growth rate continue. And we have a very high participation rate on NDAs. So this is very positive portfolio but there's lot of runway ahead of us in that area.

Bernard J. Birkett

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

We've also seen growth in other high-value products. So, with CZ, FluroTec, our new self-injection system. So we're – we've seen growth – strong growth in all of those areas through Q1 and it's represented in many of the – in the various market units, it's not just in one market unit.

A

Q

Great. Thanks for the detail. I had maybe a follow-up question. The company had a really strong first quarter, but revenue guidance was reaffirmed. And so I was wondering if you could give us some of the puts and takes of that guidance in the context of how strong Q1 was?

Eric Mark Green

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

Yeah, let me start and then Bernard will talk a little more about the puts and takes. I just want to caution – I mean absolutely when you think of – you look at the resiliency of the business and how the team is executing well under these circumstances, and I do truly believe the tenets that we put in place from the market-led, the globalization of the operations, digitization which is allowing us to get better analytics and real-time information, it's really allowing us to drive growth and we saw that – similar growth in Q1. We saw that in Q4 of last year and so we believe its continuation. But frankly speaking the operating environment that everybody is in today is difficult and so we want to be – my point of view you, we want to be prudent and stick with what we've guided. I know there's some additional elements to that that Bernard will go through and we'll get more data points over the next several weeks and months, so that we – next time we have this call we can get better information on how the trajectory will go through the balance of the year, but Bernard you want to give some puts and takes there?

A

Bernard J. Birkett

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

Yeah the – and the other – the other piece on that you got to remember is the FX headwinds that we have forecasted has moved from \$15 million to \$26 million. So if you take that into account, we're absorbing that while maintaining guidance between \$1.95 billion and \$1.97 billion, so essentially it is raising the guidance on revenue. And as Eric said it's still early in the year. We're in unprecedented times with a lot of unknowns out there, so again we felt it was the right thing to do to maintain where we are and see how the remainder of the year progresses. But what we're seeing is our order book is solid, our manufacturing and operation units are functioning as they should and in line with our expectations and we weathered some storms in the first quarter. But again I don't think it's appropriate to raise it much higher at this point. We got to think – we got to remember that a piece on the FX.

A

Q

Great. Got it. Thanks for the color.

Eric Mark Green

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

Thank you.

A

Operator: Thank you. And our next question comes from the line of Juan Avdeno (sic) [Juan Avendano] with Bank of America.

Juan E. Avendano

Analyst, Bank of America Merrill Lynch

Hi. Hello, good morning. Congrats on the quarter and thank you for the role that you're playing through this pandemic.

Eric Mark Green

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

Yeah. Thank you, Juan. Really appreciate that.

Juan E. Avendano

Analyst, Bank of America Merrill Lynch

I guess my first question is you used to give us an update annually on your participation rate across your different customer segments. Can you give us such an update for 2019 across Biologics, Generics and Pharma? And related to this question, I know that this is a long-term opportunity on the COVID-19 vaccines, but what participation rate do you anticipate to have among COVID-19 drugs and vaccines that are currently in development?

Eric Mark Green

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

Yeah. Well on this – on the participation rate last year 2019, I'll put it this way. Our Biologics participation rate was higher than it has been – or [indiscernible] (32:46) little bit higher. So it is closer to 100% you can get. And then in the Generics and in the Pharma space we actually improved. So our participation rate is beginning to improve. In regards to the COVID-19, specifically around vaccines, as customer – we won't give out customer names, but I can tell you that we're on many of the products that we currently develop and we'll be going through clinical trials hopefully soon, so that we can participate on that. I think this is why we have a good very strong participation rate in vaccines is one of the characteristics required is the [ph] coating on the elastin (00:33:30) and the FluroTec technology is a market leading technology. So we're feeling really good in that regard.

Secondly around that, when we started thinking about the criticality and the urgency to get these [indiscernible] (00:33:46) manufactured, it gives us the ability of flex our global operation and as we're building 40-plus-billion components a year, the demand on vaccines [ph] while it's important, it's a good size, but it's not going to see us with challenge (33:57) considering we have multiple sites that can produce these products using FluroTec coating. So that's how I would look at it from the vaccine perspective part of the [ph] participation rate. (34:16)

Juan E. Avendano

Analyst, Bank of America Merrill Lynch

Got it. Thank you. Your backlog of committed orders on Proprietary Products, it did increase by 44% year-over-year and 2019 according to your 10-K that you filed. I was wondering if you could give us an update on your backlog of Proprietary Product orders that are committed as of the end of the first quarter, what the magnitude of the change has been. And can you remind us what your average production lead time is from the time you receive an order until you produce it and ship it?

Eric Mark Green

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

A

Yeah. So we won't update the quarterly number, but I can say it's solid, it's consistent. In fact, with some of the discussions that we're having in regards to products used for therapeutics and/or vaccines, that will ensure that that number stays solid. I think from a range on lead times, I think the team's done a great job if you think about where we are today, and we monitor this on a weekly basis, we're about 8 to 11 weeks on average. It is based on the products and the additional capabilities that we provide around that, but I would say we're pretty stable at 8 to 11 weeks at this point in time.

Juan E. Avendano

Analyst, Bank of America Merrill Lynch

Q

Okay. Thank you.

Bernard J. Birkett

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

A

[indiscernible] (00:35:41) also taking into account that the order patterns from customers is changing slightly, customers are actually placing longer orders with us. So, it's not just one or two quarters, it's actually out over three, four quarters and maybe beyond. So, [ph] being (00:36:02) positive with that [ph] is that it (36:02) gives us a lot of greater visibility and being able to meet customer demand within the lead times of the 8 to 11 weeks on average.

Juan E. Avendano

Analyst, Bank of America Merrill Lynch

Q

Okay, good. Can you tell us what's embedded in your guidance – revenue guidance for 2020 as far as the outlook by customer segment? I mean, Biologics, Generics and Pharma, what revenue growth do you expect?

Bernard J. Birkett

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

A

So, on Biologics, we're looking at double-digit growth; Pharma will be low to mid-single digit; and then Generics is mid to high-single digit growth. Contract manufacturing will be high single digit, possibly, early double-digit growth.

Juan E. Avendano

Analyst, Bank of America Merrill Lynch

Q

Got it. Thank you. It seems that the pricing contribution in the sales revenue growth in 1Q was 1.5 percentage points, which is a little bit higher than your historical average. Can you talk about the pricing dynamics on high-value products maybe and your components, and how much pricing you can get given this environment?

Eric Mark Green

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

A

Yeah, I think – when we look at pricing, it's plus or minus 1%, historically, after the last three or four years. You're right, at 1.5 percentage points, it's a little more on the higher end of that, so it's a very – it's not a big variance. But I think what we're seeing right now, when you think about the growth that we're seeing in high-value products, particularly in the areas that Bernard and I spoke of, these tend to be new molecules. So when we bring a customer onto those products, the price contribution doesn't kick in until a year or two later, right, so that anniversaries out from a new product status.

So we're about 1.5 percentage points in the first quarter, it'll be plus or minus of that going forward. And I think we're able to maintain our pricing structure when you consider that our focus is to convert more customers to the higher end of high-value products.

Juan E. Avendano

Analyst, Bank of America Merrill Lynch

Q

Okay. Good. And my last one if I may, I mean not to nitpick, I mean you're getting good margin expansion driven by your high-value product conversion and the good organic growth on Proprietary Products, but the gross margin did come in a little bit light relative to my estimate on the Contract Manufactured Products segment. I guess my question is when could we see mid to high teens gross margin in that segment relative to how it was before – 2017 and before?

Bernard J. Birkett

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

A

Yeah, in Q1, we had some costs that we absorbed [ph] across (00:38:58) all our operational units and there was a particular impact in CM regarding supporting employees as we go through COVID-19. So we have incurred some costs there and that was a decision by management, and it is the right decision to do that. If we exclude those costs and it was business as normal, our margin in CM would have been north of 15%. The impact on the Proprietary business was a lot less, but – so that gives us encouragement to know that we're on the right track and our teams are delivering within contract manufacturing. To get to the mid to high teens we will be making progress throughout 2020 and into early 2021, but we are on the right track. I mean, there were one – there was one-time cost.

Juan E. Avendano

Analyst, Bank of America Merrill Lynch

Q

Okay. Sounds good. Thank you very much and I'll follow up offline. Congratulations.

Eric Mark Green

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

A

Thanks, Juan.

Bernard J. Birkett

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

A

Thank you.

Operator: Thank you. And our next question comes from the line of Courtney Owens with William Blair.

Courtney Owens

Analyst, William Blair & Co. LLC

Q

Hi guys. Good morning.

Eric Mark Green

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

A

Good morning, Courtney.

Courtney Owens*Analyst, William Blair & Co. LLC*

Q

So my first – good morning. My first question is around the updated kind of top line guidance. I know you kind of answered this a little bit earlier for somebody else's question, but just wanted to kind of talk more about like on the organic side, so you guys started the year very strong and I think in your prepared remarks Eric you said that you guys didn't really see any COVID related revenues yet in Q1, so it's probably hard to say from your vantage point but is really I guess if you kind of look at the rest of the year that confidence that you have that you guys will be towards the higher end of your organic – or your long-term organic guidance of that 6% to 8%, is that driven by just like the base demand for the business or is it more so related to the COVID related like incremental demand or kind of if you have to take between that mix which side does it more fall on that you have that confidence that you'll get to that 8% as opposed to the 7% to 8% that you guys talked about last quarter? Thanks.

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

A

Yeah. Courtney, I wouldn't say that the confidence is on the base business – on the core business. We are aware of additional opportunities when it comes to the COVID-19 and the solutions our customers are working towards. So this is a fluent, dynamic environment in regards to which therapies or therapeutics and/or vaccines will get through and what time – at what time. And so when we have better visibility and clarity around that, then we'll bring that into the discussion.

On the CM side, it is a little bit higher in Q1 than we – than we traditionally would see. And I think that will come down a little bit from back to what Bernard said earlier at the full year probably looking at high-single digits, maybe touching the 10% mark. But on the Proprietary side, the underlying core business, [ph] when you look at Q1 and (42:08) Q4 of last year and the momentum that has been built up [ph] around (42:13) the core has been relatively consistent. So it gives you confidence that the guidance that Bernard walked us through is really taking a lot of the opportunity of COVID-19 out.

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

A

Really it's hard to estimate [ph] that now, (00:42:30) there's a lot of discussions around COVID but we need to see something more concrete and probably get more visibility as we progress through the second quarter I guess and we'll give you a better insight into that I think on our Q2 call but it's still early. There's a lot of moving pieces in that area.

Courtney Owens*Analyst, William Blair & Co. LLC*

Q

Okay. Got it. Thanks, guys.

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

A

Thank you.

Operator: Thank you. And I'm showing no further questions at this time. So with that I'll turn the call back over to Quintin Lai for closing remarks.

Quintin John Lai

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

Thank you, Andrew. 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 Investors section. Additionally, you may access a replay through Thursday, April 30 by using the dial-in numbers and conference ID provided at the end of today's earnings release.

That concludes this call today. Stay safe. Stay healthy. Have a nice day.

Operator: Ladies and gentlemen, thank you for participating in today's conference. This does conclude the program and you may all disconnect. Everyone, have a wonderful day.

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