

14-Mar-2023

West Pharmaceutical Services, Inc. (WST)

Barclays Global Healthcare Conference

CORPORATE PARTICIPANTS

Eric Mark Green

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

OTHER PARTICIPANTS

Luke Sergott

Analyst, Barclays Capital, Inc.

MANAGEMENT DISCUSSION SECTION

Luke Sergott

Analyst, Barclays Capital, Inc.

Ready to go. All right. Good morning everybody. Thank you for joining us. I'm Luke Sergott, I cover Life Science Tools Diagnostics here at Barclays. With me, I have the pleasure of Eric Green, CEO, Chair of the Board and President of West Pharmaceuticals. I think you guys have [indiscernible] [00:00:18].

Eric Mark Green

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

[indiscernible] (00:00:19). Appreciate the invitation here to the Barclays Healthcare Conference. [indiscernible] (00:00:29) looking for the great list of one-on-ones today. Great.

Before you start, I do want to [indiscernible] (00:00:38) find on the deck posted on our website, also posted here on the screen. Let's get started about West. And April 14 is a pretty major milestone for us at West. It will be a 100 years of our existence. And it's been [indiscernible] (00:00:58) around supporting patients across the globe. We think about the level of innovation, the global expansion and where we are today in this whole process over the last [ph] several (00:01:11) years. What keeps us excited at West is that it's not really just looking back [indiscernible] (00:01:17) and what has been accomplished, [indiscernible] (00:01:20) healthcare going forward. So, it's a very exciting time right now for us globally around West. And it's the past for individuals that participated with West current and also the future.

Let's talk about our business, a little bit know the story. We're very clear about our purpose and we're a purpose driven company. It's about serving patients. It's improving patient lives. We are a critical manufacturer in healthcare. We did about 47 billion components last year and each and every one of them we feel is high level of quality and the purpose drives us to make sure that each and every one goes out as thinking about the patient names on that one product. We have a very clear strategy. We'll get into greater detail, run, execute, innovate and grow and this has been our framework in our business for last several years and it continues to serve us well [indiscernible] (00:02:21) globally.

Simplistically, if you want to break our business from a product point of view into three buckets, what does West do? At West, we are a major manufacturer of vial containment and syringe components. We're involved with administration products. If you're in the hospital setting, you'll see our products used on a daily basis. And obviously, we have moved more in towards drug delivery and diagnostic devices. This gives us a very strong foothold when you think about being the leader at containment and delivery of injectable medicine, very attractive space in healthcare, it's a fast growing space of healthcare and we're very well-positioned with a pretty broad portfolio build to service our customers.

The diversity of our portfolio, think about it from three different angles. One is from the geographic point of view, over 50% of our revenue is outside of the United States in the Americas. Thinking from a product category, not too many years ago, I would sit here and talk about 30% or 40%, but now 60-plus percent of our business in what we call high-value products, the small components and delivery devices that we provide our products and that's one of the main thesis of the growth algorithm at West, which I'll talk further.

What was also very exciting is that our participation across all the different categories of biologics, generics and pharma continues to be very strong. Biologics is over 40% of our total enterprise revenue today with about 17% of contract manufactured. 2022 was a significant year for us. There's a lot that we have accomplished. One, over 47 billion components we delivered to our customers across the globe. Two, as we expanded our product portfolio in many different ways, most notable is that we're moving from a component to system approach, and the partnership with Corning gives us technology and capabilities that we did not have in our portfolio that we're willing to expand on. We added new products to the portfolio and expanded lines around SmartDose and Crystal Zenith. And it's also important to note that we continue to expand capacity and think about investing capital into the enterprise where best to redeploy the cash that we generate is back into the organic growth story that we have at West. Significant capital expansion is going to [indiscernible] (00:04:54) whole global network.

And lastly, it's important for us to continue to [indiscernible] (00:05:00) the communities where we live and work. We truly believe it's part of the DNA of West. It started back with our founder, Herman O. West, and we continue to dedicate time and resources to support our local communities, which also drives our ESG strategy, which is not a initiative, it's built into who we are into our framework as a business.

We talk about market-led. What does that mean? Market-led is when you think about from a customer in a commercial perspective, it's identifying what are the unique value propositions we need [indiscernible] (00:05:38) bring to the table to expand our portfolio and capabilities that gives us differentiation and helps our customers deliver those critical components of the drug molecules to patients across the globe. It also informs our R&D, our technical area of our business to how do we broaden our portfolio to be more effective versus inwards out, it's out in concept. And also this market literally has allowed us to globalize our operations to really level load and be more effective to leverage the assets we have across the globe.

So, when I think about, starting with the first part of this is around the market-led approach on a commercial side. We have a very healthy participation in all areas. As you know, an injectable space is roughly around low-single-digit volume growth. The fastest growth of the injectable space is around biologics, and our participation rate in biologics is extremely high. And as you think about whether it's the innovative biologic for biosimilar, we view that as consistent [indiscernible] (00:06:50), our value proposition is very, very similar. And to think about our participation in biologics and what has that resulted is that in the last five years, we've gone from about 20% to 40% of our revenues are generated by the biologic space.

If you think about the number of BLAs, pipeline and our participation in the pipeline as it comes out to be commercial, we're in a very strong position to continue to have accelerated growth [indiscernible] (00:07:20) top

line of our business. And we're also driving, what we call, high value product portfolio and it has taken customers on a journey from the lower bottom section of the chart all the way to the upper right.

As we think about new drugs, [indiscernible] (00:07:34) biologics and some other unique molecules and small molecule areas, we're pushing – we're discussing with our customers around NovaPure. [ph] We're proceeding (00:07:45) the market with around NovaPure with higher end of the trajectory of this portfolio. And we're also now getting involved with devices and these devices we have four [indiscernible] (00:07:57) last several years we have now wearables for [indiscernible] (00:08:02) combination devices with wearables which is exciting as you think about the smart shift between IV to subcu. We're in a very good position to support that transition and for our customers and ultimately the experience of the patient.

Clean bioscience, it's interesting – when you think about where we – we just opened up a new R&D facility last couple of weeks ago in Pennsylvania. What's exciting about that facility? It's really driving more materials sciences [indiscernible] (00:08:34) direct interaction materials allowing us to identify what is the next generation of portfolio [indiscernible] (00:08:42) to drive value to our customers.

So, we do look at the portfolio expansion. We're continuously looking at the technologies that we're scouting for, which we will bring them in as we've done in the past several years, and we're also looking at product lifecycle management. So, those are the key levers and drivers we're looking at within R&D and delivering as we go forward.

One area of growth when we're talking about top line growth is our algorithm for the top line is 7% to 9% organic growth. And when you think about the drivers of that, obviously, biologics is the fastest area of growth in that area. It's being led by a high value product portfolio. COVID had impact on our business. I believe we as an organization responded significantly in order to help with the pandemic, provided critical components of use to really deliver the vaccines across the globe. So, West had a very important role in that process.

If we take that out of the equation, the organic growth of the base business which you'll find here since 2020, has been growing in the double digits. That's taking COVID out of the equation. And most of that growth is around high-value products.

What you'll find is that during that period of time, there was a margin expansion that naturally through mix shift that occurred. As we think about specifically, we mentioned on the February call that COVID was about \$388 million of our business in 2022 and we estimate, at this point in time, about \$80 million, \$85 million will be COVID. So, you can see a headwind of about \$300 million and we're projecting growth in 2023, organic growth, in 2023 a number of initiatives that we've launched, a number of the demand-pull effects of the non-COVID business that we can see here continues to grow quite well. And we anticipate that continue on.

From a margin perspective, so the growth thesis of West is 7% to 9% organic growth on the top line, and about 100 basis points operating margin expansion year-over-year. Again taking COVID out of the equation, in 2019, our operating margins were roughly about 16% and this year, we're targeting 2023 to 2024 [ph] – implied (00:11:15) 23% to 24% operating margin. A significant growth without COVID has been taken out of the equation.

Why is it important to when you think about the margin expansion, the majority of that is mix shift due to the high value products? Think about the number of products we produce every year, 47 billion components, roughly about 20% of that is high-value products, but that equates to over 60% of our revenues associated to high-value products. But every year if you assume, if you look at the model, it's roughly about 100 basis points expansion on units of high value products due to new drug launches, conversions, growth in the biologics space in particular.

That gives us about 100 basis points of units expansion on that 47 billion. So, when you think about how that translate into top line revenue, you see here, clearly it's accelerated from the mid-40% to mid-60% over that same time period.

So, as we go forward and continue to [indiscernible] (00:12:30) the market, [indiscernible] (00:12:31) around the fastest areas of injectable medicine, where we believe that we'll continue to able to leverage our organization with a mix shift and other initiatives like automation, pricing, gives us continued expansion on margin here at West. When we globalize our operations, we're now able to be more effective to level load the demand. And today, we have 26 manufacturing sites across the globe, five of which are heavily focused on high value products and processes. And so, what we have effectively done is drive more efficiencies through our global operations. We have more opportunities ahead of us. I'd say early on in the automation journey and we're excited that this is an enabler for us to support our customers and mitigate risk of their supply chain and continue to appreciate the high participation rate in all different areas of biologics, generics and pharma.

Talking about expansion, this last couple of weeks ago, I went to our Kinston, North Carolina facility. We actually had a tour of investors that came through, and we are literally almost doubling that site. The HVP plunger expansion is on its way to be completed in the second quarter validation and we'll be able to support the demand that already exists with plungers around HVP, particularly around NovaPure. And also HVP processing capabilities will be done later in the year. We have a number of key initiatives that are underway to be able to invest on the organic growth here at West and across the span of the globe. What you'll find though almost with concentrated, one, around high value products, and two, around these five sites that we have designated for HVP globally.

Thinking about the use of cash. Since 2016, we deployed over almost \$2.5 billion of cash into various sectors of our business. The number one area that we have, about 50% of it, we focused around the capital expenditures expansion. And you think about our CapEx of \$1.2 billion, in the last few years, what you're seeing is that about 70% of our annual CapEx is being deployed for growth initiatives. While the other 30% is around maintenance, around IT infrastructure. Historically before few years ago, we were about 50-50, and it's heavily weighted towards higher growth. And the guidance we gave for 2023 was roughly around \$350 million. Again, around 70% of that is growth orientation. The other area of investment of that cash has been around inorganic to complement our organic growth story. We have done a couple of transactions that have allowed us to get license, equity and further enhance partnerships. One in particular this year has been the 50th year of partnership with our Daikyo Seiko in Japan, a phenomenal company that we've been coexisting for a long time. And they're able to leverage our technologies on both fronts to really, truly differentiate in the market.

Obviously, when you think about giving back to shareholders quarterly dividend and then the share repurchase. And in the last five years, we've been focused on share count neutrality. So basically, keeping the share count neutral. And as you can see here, we have succeeded over that time period. And one area that I think the organization has done a great job is this transition into more free cash flow in the organization and cash. So as of the end of 2022, our net cash was close to \$700 million. And this gives us very strong footing as we think about the growth here at West. Now, last month, we did approve \$1 billion share repurchase program, which is obviously larger than we've done historically. We do not have a specified expiration date, but one of the key themes there is that we are going to continue to keep the share count neutral and then deploy at appropriate times additional repurchase throughout the next several multiple quarters. And again, there's no expiration date on that.

As I said in the beginning, we're driven by purpose. And one of the areas around ESG is you think about our strategies. These initiatives are built into the fabric of our organization. These are not initiatives [indiscernible]

(00:17:45), that ended up they're managing, it's part of who we are, and it's been part of us for a very long time. We have six key priorities for 2023 and beyond. These are pretty typical. I think you'd think with a lot of firms and we're making great progress in many cases, we're actually ahead of the programs. What's exciting is that not only and we will have a publication coming out shortly so you can look for Corporate Responsibility Report that will be published, 2022, in the next several weeks. But what's exciting at West is that this is a continuous process improvement mindset. We're kind of continues to look at ways to make an impact. One area I'm extremely proud of is just an example is our safety program, where we have really literally cut it in half twice in the last five years, which provides a better environment for all of us, a safe environment to work across the globe here at West.

So to conclude on the discussion here, really, West is in a very strong critical position in health care. Our participation rate on these new drug molecules remains very high. We're excited about the future of injectable medicine space, particularly around biologics. And we continue to leverage our global operations to truly differentiate and to build, to meet our customers demand and needs, not just in the near term or long term. We're investing in new technologies and new capabilities. They'll give us another look at from components to systems. As an example, I'm really excited about that initiative to really create another wave of high value products for West and also our pull effect that we're having in the wearable space and injectable medicine space that we believe we can be a major player from the IV subcu phenomenon that is going to occur and support patients again across the globe. We've a very strong balance sheets. We have strong opportunities to continue to invest in our business, but also look at all adjacencies. And we'll continue to stay focused on each and every component that we produce has the patient name on it.

So, thank you for your time and I appreciate your interest in West and we're available to take any questions. Thank you.

QUESTION AND ANSWER SECTION

Luke Sergott

Analyst, Barclays Capital, Inc.

Great. Thanks. Any questions?

Q

Q

[indiscernible] (00:20:19-00:20:26).

Eric Mark Green

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

We're very, very high in that area of roughly 90-plus percent in biologics. We also, just to be very clear in our communication, is that we also classify biosimilars in the same category. The value proposition is the same. Similar products, similar economics. So, we're very strong in the biologics space.

A

Luke Sergott

Analyst, Barclays Capital, Inc.

And you had the slide up there on the high value products. Talk about what you guys have from cell and gene therapy perspective because it's a different delivery model versus anything that's been out there. And so, how you see that ultimately shaking out and where you guys are positioned?

Q

Eric Mark Green

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

A

Yeah. Currently, we do participate in cell and gene therapy. We are positioning our Crystal Zenith portfolio. Obviously, NovaPure in addition to that. So, we are participating in all the delivery of those products. The volumes are not anywhere near other type of therapy classes. But we are participating in that area as we are continuously also looking at ways to expand that capability to go beyond just containment.

Luke Sergott

Analyst, Barclays Capital, Inc.

Q

Right.

Eric Mark Green

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

A

So, that's where we currently are, but we are participating in every CGT.

Luke Sergott

Analyst, Barclays Capital, Inc.

Okay. Okay.

Eric Mark Green

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

Thank you very much.

Luke Sergott

Analyst, Barclays Capital, Inc.

Thank you.

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