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Presentation

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Good afternoon and welcome to Ontex's Investor Update. I'm Geoffroy Raskin, the successor of Philip Ludwig, who is with us here today, and I'll be your contact for an Investor Relations going forward. I have a couple of practical comments to make first. The presentation can be downloaded from our website or from the webcast landing page at the right side of the player. For those of you who wish to participate in the Q&A, you need to connect through the Zoom platform. The details of which are described in the press release, but you can also find it on the right side of the player in the webcast. Obviously, we are issuing forward-looking statements and I remind you of the disclaimer in this presentation. But without further ado, let me pass you to our CEO, Esther Berrozpe.

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

Thank you, Geoff. Good afternoon and welcome to Ontex's investor update. Thank you for joining our video meeting this afternoon. For this investor update, I am joined by our CFO, Peter Vanneste, who most of you know, and also by Laurent Nielly, President of our Europe division, and Vincent Crepy, Chief Supply Chain Officer. Our aim today is to update you on our strategic priorities and the execution of our strategy. I will begin and then pass the floor to my colleagues to give you more color on their areas of responsibility.

As you will have read in our press release earlier today, we have finalized the key decisions that will form the foundations for the future of Ontex. First, we have decided that the route to value creation is to focus on what we do best, serve our partner brands and healthcare business in Europe and North America, and we have started operating accordingly. Secondly, we have defined where the structural cost base should be for the group to win in the market, leading to an extended savings program. In the short term, we remain fully focused on the elements within our control and we have made significant progress in 2021 against the backdrop of a very, very challenging environment. We have seen sequential top line growth since the beginning of the year. Secondly, our restructuring and cost savings plans are delivering as we targeted for the year. And lastly, we have maintained strict cash discipline and directed CapEx only to the investments required to drive profitable growth. In this context, we have accelerated our plans and I am very confident that Ontex will come out of the crisis stronger and more profitable.

Turning into the next slide, the current operating environment. The situation is extremely volatile leading to very poor visibility of what is ahead of us. I am not satisfied that we have had to announce that our margin expectations for the full year are lower than what we expected at the end of October. This is very disappointing and illustrates the challenges we face at the moment and the need to bring our structural costs down. The exceptional post-pandemic GDP growth has caused unprecedented increases in raw material prices, energy, and transportation costs, as well as disruption to our logistics and supply chain in general. The extent of the inflation in raw material prices has been unprecedented. As you know, indexed raw materials form the largest part of our product cost and the increase of these indexes varies between 40% and 80%. We have also experienced significant inflation on other raw materials and operating costs. Examples is packaging up 50%, energy up 250% for gas and 180% for electricity, and sea freight up threefold. These challenges have intensified throughout the year and the pressure has steadily increased on both the top line and our margins. Turning now to the measures we are taking to mitigate this impact, in other words, the elements where we have full control.

So on slide 6. To offset the input cost situation and rebuild our mid and longer term value creation, we have two levers: cost reduction and pricing. So, firstly, cost reduction. We are extending and accelerating our cost reduction program to deliver a year-on-year cost productivity of 4% going forward. This new approach differs from the past at Ontex as we are changing the fundamental cost base to bring down our breakeven point. This will make our group leaner and more agile for the future. Both Vincent and Peter will talk more about this in a minute. To tackle the headwinds of 2021 and what we expect to experience in 2022, we are targeting €80 million of gross cost savings, adding to the €75 million cost reduction in 2021. Secondly, pricing. Given the extent of the increase in our input cost, we are planning to pass some of these on to our customers. There are early positive signs in the market as we see A-brands increase in their prices. And this will provide the headroom for retailer brands to increase prices as well. Laurent will talk in more detail, but we have a customized approach customer by customer. And we look not just to increase the prices, but to optimize the product offering and to generate efficiencies across the value chain without impacting the quality of our products. Pricing actions will be taken across all our businesses.

In June, we set out three financial targets for 2023. And these targets remain unchanged as an ambition. We will get to the 2023 targets, thanks to the execution of our plan and portfolio divestments that I will talk in a minute. And then, Peter will come back in more detail on the scenarios we are working on today. Let us now talk about the group's portfolio.

When I joined Ontex at the beginning of this year, it became very clear to me upfront that our business was way too complex and our resources were being spread too thin. These have prevented us from supporting appropriately our core businesses. At that time, I said the objective of simplifying and bringing focus to our business and product portfolio. Ontex has been trying to deliver value on two fronts for a number of years now without success. On the one hand, Ontex wanted to be the partner of choice for retailer brands, lifestyle brands and institutional clients in developed markets. And on the other, the group has worked to build Ontex's own brand positions in several emerging markets. This resulted in the group losing its way in its extremely strong position in Europe, and performance has been affected. Furthermore, the emerging market positions have not generated the returns on investments required. Therefore, we have decided to refocus Ontex on partner brands and healthcare. And by partner brands, I am talking about retailer brands or private labels, sometimes called. Lifestyle brands are premium brands that appeal to an aspirational way of life. They typically use natural materials which are good for you and societal benefit value proposition. These brands are growing very strongly in both North America and Europe. Lastly, in healthcare, we serve institutions and distributors with a very similar business model compared to the partner brands. This decision automatically brings geographical focus to Europe and North America, where partner brands are well-established, sizable and offer the greatest potential for profitable growth. This new focus will enable Ontex to continue to leverage scale benefits from raw materials to production, logistics and, of course, in our go-to market, including customer service. In this way, Ontex can excel once again with a strong customer centricity, offering innovative products with best-in-class quality, cost and service. Leveraging off these economies of scale will reinforce our goal of always being the partner of choice for our customers.

And to maximize the opportunities created by this decision, we can leverage off Ontex's inherent strengths. We will focus management time and capital on our core businesses in Europe and North America markets, which are attractive due to their size and growth potential. Just to bring some perspective, in 2020, these markets accounted for €1.4 billion of revenues being around 70% of the revenues of our group. They generated an adjusted EBITDA margin of 13%, being close to 80% of the overall margin of the group. This is where we will focus our development attention to drive growth and mix and make the necessary investments in research and development and manufacturing capabilities. Going forward, we will manage the operations in the rest of the world for value and cash. In 2020, these businesses that are outside Europe and North America had revenues of €600 million with an adjusted EBITDA margin of 8%, well below the group average and value-creation expectations. These activities are under review to determine the best path forward with advisors already appointed. We will, of course, update you if and when any decisions will be made. We can now focus our attention to restoring growth in Europe and accelerating our development in the US.

In Europe, we have seen sequential top line growth since Q2 this year and two primary objectives here. First of all, strengthen our leadership position to be the partner of choice once again. And second, accelerate the focus on faster-growing margin-accretive products and this includes all adult care products, baby pants, products with natural materials, and online channels. Laurent will tell you more in a minute about how we are bringing the business in Europe back on track. In North America, where the market has great potential for partner brands, the objective is to deliver sustained double-digit profitable growth. We will accelerate our development, building on our strong foothold. And our new US plant is coming on stream, which together with our Mexico operations, will give us a coast-to-coast capacity to supply all our customers.

Now, I would like to introduce Laurent Nielly, President of Europe Division, who will explain in a little more detail the dynamics of the European market.

Laurent Nielly
President Europe Division, Ontex Group NV

Thank you, Esther; and good afternoon to all. I joined Ontex four years ago in Brazil after the acquisition we made in Brazil. And through my 30 years of career, I spent a number of position in finance, commercial and general management capacity in consumer good companies like P&G, PepsiCo and Coty, where I acquired experiences in driving growth, turning around businesses in both stable and volatile markets. I joined the executive management team last February. And since then worked to stabilize Europe while restructuring our commercial organization, combining our two previous divisions of Europe retail and healthcare. Now, as mentioned by Esther, the key task at hand, in addition to driving more pricing initiatives, is to return the Europe business to sustained growth by stopping the share losses on our retailer brand part of the business, which have mostly done by now, and by repositioning our portfolio to increase our exposure to the growth pockets.

So first on the retailer brand turnaround. As many as you know, this is a unique business model. The way to drive retail brands and, by the way, most of our institutional tender business and adult care is different. First, it is a business governed by sales contracts and in most cases, subject to tenders. Second, the interactions with our customers are mainly product specific, based on performance, requirements within a defined price target. Third, versus the regular branded business, the levers that you can pull are different. It is harder, for instance, to stimulate short-term demand. Some customers, of course, are more sophisticated in the way they build their brands, and you de facto, have more you can influence but many others do not. And if you combine this with the fact that the contracts on average last two to three years and are re-tendered nine months before start of new shipment, you have a certain inertia. So you have to address it in a complete way, working on assortment, on mix, product specification and chasing down non-added value costs through the entire value chain customer by customer, something we have ample experience of. And as we've already shared in the past few months, after four years of net losses, we are turning the corner while addressing all the fundamentals from the way we prepare tenders, we serve our customers and help them grow.

It is hard foundational work and we know how to make it work. Let me share two examples. The first is a continuation of the story with our top Poland customer that some of you may have heard previously. This is a demonstrated win-win approach to a partnership where we invest in dedicated teams and innovation, together with our customer, help grow, share and strengthen the brand, which you can see on the left side of this slide. The second example is one of a comeback, an important customer that we had lost most of the business with in 2018. We had to rebuild it by regaining trust, relationship, delivering the basics and demonstrating we could help our customer change its trajectory and thereby change our penetration within its business. But as you can see, it takes time, linked to the inertia that I explain. So we cannot only rely on net gains and losses, we also have to improve our portfolio growth exposure.

And that's the second part of the change of our trajectory, which indeed will come from us outgrowing in a few areas that we have prioritized and that we want to accelerate. First, improve our position on the growth pockets of the baby markets, namely the pants and the eco sustainability solutions. Second, outperform in adult by improving our presence, and help our customers in winning more consumers entering the category. Third, trade up through relevant innovation and portfolio mix in all categories and especially in fem care, where we will focus on where we can profitably make the category more attractive to us with some synergies with our North America business. And finally, across all categories, step up our presence online directly or through our distributor and retail partners. For every of these priorities, we have a multiyear plan. For baby pants, for example, we have worked on improving our products which we have mostly rolled out by now, sharpening our shopper-led story to unlock growth with our customer, which we say is our playbook. And we, in parallel, aim to reduce the cost gap between pants and open diapers while investing into more capacity. But I want to expand a little bit more in adult, which is Europe clear growth engine.

Adult category is the largest business of our combined Europe division. We are holding a strong number two position in Europe and through that and our presence across all channels, we are well-positioned to win in this margin accretive category. To accelerate our growth, we will maintain our strong position in the healthcare institutional channel on one hand, while accelerating the expansion in retail on the other hand. In institutional, this means providing more service solution over time, but also improving our presence in what we call self-pay, which is the channels on which consumers can decide and pay for themselves the product as opposition to the reimbursed channel in which the consumers receive an allowance to cover the cost of the product. Importantly, to be able to do that, we will have to protect our equity with the caretakers and the institutional channel players that are key to build what our brand is today, by respecting our roots, segmenting correctly our brand and portfolio, bu also by testing several service offering. One of them that we've already shared in a couple of occasions, which is our connected diaper solution which we call Horizon. On the more traditional retail side, it's about helping our customers to make the category more relevant, especially in the point of entry of the category, which are the light inco and pant segments. As you may know, this category had a lot of consumer taboo for a long time, but we see those taboos being reduced over time and the penetration of the category increase as consumer acceptance grows into shopping for those products. And then, of course, we are working to increase our online presence, but not just for adult, across all the categories.

Finally, a word on innovation because this will continue to be one of the key driver for our growth. Being able to fast follow branded leaders, as well as providing consumer-relevant, cost-effective solutions and differentiation options for our customers remains key. We have already refocused our innovation effort based on the category-focused set of Center of Excellence, which are the blue bubbles that you see on that map. And at the same time, we have already streamlined our teams of R&D. So, we will be able to tap into the depths of our R&D teams, our engineering and supplier knowhow to develop those product platforms. And we have clearly separated those design teams from what we call our local adaptation teams. This allows us to better prioritize, ensure that we drive scale, and balance our efforts between design for value and new benefit-led innovation. This will also allow us to continue to win tenders and improve the mix towards higher-margin products.

I wish I would have more time to give you more insights into our business. But I want to thank you for the opportunity to share a little bit of our journey in Europe. We have a very good base to build off and we are clear on the direction, as well as have a high sense of urgency to improve our top line performance both on pricing and on volume. We have decided where to focus and where to invest to accelerate growth. We know what winning looks like and we are in the process of rebuilding non-negotiable table stakes. Let me now give the words to Vincent Crepy, our Chief Supply Chain Officer, who will provide you with more insights into how we intend to drive cost and service excellence through industrial transformation. Vincent?

Vincent Crepy
Chief Supply Chain Officer, Ontex Group NV

Thank you, Laurent. Good morning and good afternoon to all. Now that we have seen how we are going to deliver our ambition in Europe, let's see our industrial transformation agenda is going to support our strategy. So a few words about myself. I have joined Ontex relatively recently in May of this year in the position of a Chief Supply Chain Officer, which has been created to lead our supply chain truly end-to-end. My background is in consumer goods company such as Procter & Gamble and also Reckitt Benckiser in which I held leadership positions in operations in the US, Europe, Central America and Asia Pacific. I bring in knowledge and experience in the supply chain area and also a passion in transforming the business. In a nutshell, our transformation agenda is about unlocking significant value from our end-to-end supply chain, building on our network and scale, to take performance to the next level, placing consumer and customer first in everything we do, being agile, lean and scalable. And we will achieve this through a holistic and synergistic approach using battle-tested tools and methods, building a winning mindset with clear accountabilities and a laser focused execution.

So we have a high fixed cost and a very high dependency to commodity as Esther mentioned. Commodity inflation through the 60% portion of raw materials and also on other operating costs. While we have well deployed asset base close to our customers, which is critical, we also have a high level of complexity, which translates in excessive diversity of equipment with a low utilization. So, in other words, we have plenty of opportunities.

Now, to support our company goals, we want to develop the capability to deliver a sustainable 4% year-over-year cost improvement to contribute to our profitability growth, keeping net working capital below 5% of sales and CapEx in the ballpark of 4% to 4.5% of sales to secure our cash conversion objectives while investing in a disciplined manner in growth in a very focused way. We want our customers to rate us in the top tier in term of service. This is critical in general. And that's even more important for partner brands, of course. At the same time, we will secure that the quality and performance of our product is at par with international brands. And, of course, we want to do this, keeping sustainability in mind with the ambition to improve our safety and carbon emission performance year-over-year.

So we just talked about the why we have an industrial transformation agenda, which is basically to deliver the goals and objectives that we've just seen. The why is clear. Now we need to define the what and the how. The what is all about infrastructure, where do we make products, where do we ship products from and with which type of assets and the how is about ways of working and mindsets.

So, first footprint, where do we make and ship from? This is all about balancing manufacturing and transportation cost to achieve the lowest total delivered cost. Key to that is the concept of logistic footprint: the denser the product, the farther it can travel economically. Tampons, for instance, very concentrated if you wish, can be manufactured from a global site and distributed worldwide, while adult incontinence, much larger product, less dense, has to be produced closer to the consumer, typically within 700 kilometers radius. Now, let me take specific examples of actions we already took in that area. In Europe, we have announced our intention to close our manufacturing operations in Mayen, Germany. We are also moving the production of eight lines from Belgium to Spain and Czech Republic closer to the customer base. Another example related to growth in North America, as Esther mentioned, we are ramping up as we speak manufacturing capacity on the East Coast of the US, which will – and we will be the only player actually to provide customers with coast-to-coast sourcing flexibility. That's about footprint optimization.

Now, what type of assets do we want to have? As mentioned, prior, we have a very diverse asset base. We have more or less 300 lines and none of them are identical one to another. We want to streamline that to a fewer number using faster equipment on harmonized platforms. This will allow us to reduce the number of lines by 20%. And as a consequence, improve capacity utilization by 10 points over time. So, let me take a very concrete example. We have about 80 open diapers line. And over the next few years, we are planning to accommodate the current volume and the growth on half that number, and we are going to do that by focusing on the faster equipment that we have, harmonizing product features to one platform to then even further speed up the lines.

Ways of working. So in terms of ways of working, we are improving our capabilities in strategic procurement, design to value, and industrialization, the magic triangle – this magic triangle will help us to optimize material cost. Let me take a concrete example. So I talked about open diapers and we have tremendous opportunities to standardize our open diapers, as I mentioned prior. Specifically on the chassis, which is the base shape of the diaper. We are aligning on a straight chassis, moving from cutting out the shape that fits the baby to on a straight chassis, adding ears to get the baby shape. This is designed to value, removing waste. Now, reaching out to suppliers of ears was the right approach and good timing, while being able to rollout the new specification very fast, which is the purpose of industrialization, is creating even more value from the design-to-value exercise and is creating value faster. This capability to industrialize better and faster rolling out change of specification efficiently and rapidly is critical to our success.

Now, talking about waste elimination. That is exactly the purpose of our operational excellence program. Not only do we want to have one diaper design on the, example I took, on one type of equipment. We also want to have one optimized way to make it. This drives efficiency, which in turn increases utilization of the assets. Now, specifically, we have the ambition to reduce scrap by a third, 30% and thereby help to increase our OEE up by 15 points. OEE is equipment efficiency. Now we have reason to believe we can get there. As we already see in 2021, we expect our scrap to reduce by 10% and to increase our efficiency by 5 points. Now, operational excellence doesn't stop at the manufacturing lines. There are many other possibilities to streamline our ways of doing. For instance, we're actively working on increasing the number of units for pallets, optimizing pallet fit, outer case dimensions, basically to put more product in a truck. Beyond manufacturing and logistics, we want to rollout our lean and agile approach to all functions: planning, development, procurement.

Now, all these are battle-proven methods, and there is really nothing new in attacking all the sorts of inefficiencies at the roots and in putting in place pragmatic ways of working focusing on getting results. The catalyst of all this is going to be to further develop the right winning mindset, setting ambitious and clear expectations, providing proven tools and methods and holding ourselves accountable to deliver no matter what. That's going to be key to success.

So, as we have seen prior, for instance, with the example of the straight chassis, not only do we tackle the entire chain holistically, we tackle it in a synergistic manner. We look to maximize everything we do across the board. Our efficiencies will turn in improving our asset utilization, which will reduce our fixed cost and our need for CapEx and inventory to operate the business. Higher efficiencies will also enable us to use the material to the most, avoiding waste, hence further decreasing our cost, et cetera. So, clearly, one plus one equals more than two. So, we have ambitious objectives and holistic and synergistic approach using battle-tested methods to become leaner, more agile and scalable. And we are building a winning mindset with clear accountabilities and a laser-focused execution. Now, at the end of the day, the proof is in the pudding. And as a matter of fact, our full end-to-end approach creates momentum that is visible in the P&L today. Esther mentioned a few numbers. And we are building on this momentum for 2022 and beyond.

I'll pass now to Peter, who will take us through how our strategy translates int financial outcome. Thank you.

Peter Vanneste
Chief Financial Officer, Ontex Group NV

Thank you, Vincent. And good morning, good afternoon, good evening, everybody. Over the next pages, I will tie this all together and I will mostly focus on the new Ontex strategy and on how that translates into key financial metrics. So, I'll be focusing on the ambitions and the targets for new Ontex perimeter, Europe plus North America. My main focus will be mid-term. I will be touching at 2022 at several occasions, but I will come back with a more elaborate view on 2022 at the usual time early next year.

Now, as Esther pointed out, since mid this year, we and by extension, the whole sector, have been facing accelerated inflation and supply disruption in an absolutely unprecedented way. I'm surely not bringing any news to you by saying that. The extreme level of inflation is very clear from the table on this page to the left. This is showing the evolution of our main indexes as a weighted average for the last 10 years, and you can see the huge peak very recently. In our business, input costs have gradually risen 15% to 20% versus 2020. And this has disrupted our market, our sector in a very significant way. The supply crisis started to weigh on our margins as you've seen in the last quarters. You have seen in the Q3 results a year-on-year €28 million higher index-based input costs in one quarter, partly offset by €15 million strong net savings also in just one quarter. And about Q4, with the current volatile environment, the expected improvement in supply is not materializing as we saw in the fourth quarter as we anticipated. Although these problems are of a temporary nature, our revenue and bottom line in Q4 are being impacted. Versus the outlook of minus 1% like-for-like revenue decline and 9% adjusted EBITDA margin for the year, we expect both the revenue and the adjusted EBITDA margin to come approximately 0.5 point lower. Within this context, it's clear that 2022 will be a challenging year with unprecedented inflation reflected in most of our supply contracts to be gradually mitigated throughout the year. As we explained earlier, we are pricing across the business and we have strong and accelerated cost programs and we are reassured by the strong results we are realizing on them in 2021. We believe that these unprecedented levels of inflation will normalize at some point, but we're not counting on that. And, therefore, we focus on what we have under control, growing our business, accelerate the cost savings, pricing, optimization of our mix, and the portfolio changes. So, our plans and numbers in this section, therefore, do not include any softening on these extreme cost levels. We need to realize this is as a harsh assumption as there is a strong upside potential if those levels would even partly turn back to normal.

On the top line, Laurent has been showing you how the growth in Europe is being realized and our strategic plan foresees a 1% to 2% growth over the coming years in Europe. We're coming out of a difficult period in Europe with 3.5% decline in the years up to 2020, driven by some important contract losses. And the chart on the left of this page is actually measuring the sum of impacts of all contracts that we've won minus contracts that we've lost. And you see before, in the past, before 2021, there's net losses. The net balance of contract gains and losses has, however, stabilized in 2021, and shows a net positive balance going into 2022. And there is a time lag between the moment a contract is won and the actual first sales resulting from that. So this trend does provide confidence for what is coming. Shifting to North America, the second pillar of our core focus, we foresee double-digit growth over the coming years. And this is actually a continuation of the track record of 11% CAGR that Ontex realized from 2017 to 2020. With the combination of these two regions, New Ontex will demonstrate 2% to 3% growth over the next years and mid-term. That is one point lower than when we include all emerging markets from our current scope. As you've seen earlier, the core however has significantly more profitable sales, US and North America. So the strategy to focus on our core is positive on a margin level. In the near-future, sales growth rates will be higher because of the pricing that we are and will be implementing.

Next, cost. In our strategic review, over the last months, we've been stepping up our cost programs significantly to mitigate inflation on the one hand and to drive year-on-year margin growth on the other hand. In 2021, we have demonstrated our capacity to generate very significant savings. In Q3 again, we reported a total of €52 million savings realized over the year, which is gross, and net that's €42 million. And we aim to a total of €75 million for the full year, which actually represents €60 million net savings. Leveraging on that momentum, we target at least €80 million gross savings for 2022, which is more than 4% of our cost base. As we focus in the upcoming years on our core Europe - North America parameter, we have sharpened the programs and are confident that we can continue to deliver the 4% of productivity on our cost base as an annual drumbeat also after that. Supporting these programs, we require a one-off charge of a total of €170 million, €75 million of that is in 2021 already, almost €20 million above what I said last June yet all of that is non-cash. So the €75 million in 2021 contains €50 million cash, €25 million non-cash. And then after 2021, €95 million in the next two years of which €80 million cash, €15 million non-cash. The corresponding benefit to these €130 million cash is €300 million over the years 2021 to 2025, and that's the sum of what you see on the left, €75 million realized already in 2021, and then €80 million on top of that in 2022 and then 4% productivity after that. As we have extended the capacity optimization and overhead reduction programs, we already discussed in June, but we accelerated and Vincent continued to – has been talking about. So, €75 million already in 2021, €80 million already in 2022, as I said. The largest components of this investment are initiatives, first initiative to increase the capacity optimization, utilization and optimize the operations footprint. Secondly, the overhead reductions mostly in Europe, and it also includes the cost of divestments and restructuring as we pursue our strategy that Esther has been highlighting.The savings €300 million, completely outweigh the one-off cost investments and the average payback on the individual projects is about three years. It's clear that these programs are critical to offset first short-term inflation, but also as a major contributor to our mid-term target margin growth in new Ontex, allowing us to become leaner.

Now, I have talked about our top line target of 2% to 3% on the new Ontex. Let me now elaborate on the margin. As mentioned earlier, the unprecedented inflation puts short-term pressure on our margins across the group since a few quarters and requires strong cost saving and pricing to gradually offset this. Our strategic agenda is to reduce the scope and divest businesses under strategic review. Assuming a full divestment of the non-core in the next two years, and the execution of our plan on revenue cost pricing for inflation, the mid-term target level of 12.5 % to 13.5% adjusted EBITDA can be reached for the new Ontex in 2023. On all our businesses under strategic review, portfolio projects have already started, and we engaged advisors on them. And given the margin difference on core and non-core, divesting these businesses have a positive effect of about 2 points on adjusted EBITDA margin. We believe that the unprecedented levels of inflation we see today will normalize. But as I said before, we've not assumed any softening on this. And so, in this sheet, you don't see any assumption on lowering the margin from current peak levels. But just as a reference, a 5% softening of the current peak inflation levels also puts the business within the margin range by 2023 without any of the divestments. Having said that, we do have an internal target and ambition to divest at least half of the businesses under strategic review over the next 12 months. However, as we do not control all the variables in this, we will keep you posted as we're making progress. And with a new perimeter, our ForEx exposure will clearly be very much reduced. And we have been suffering from that in the past few years. Beyond 2023, the new Ontex has a margin potential of above 15% by 2025, driven by the continued business growth and saving programs, which a SG&A structure below 10%.

On the cash front, looking at working capital first, focusing on the core business and the partner brands will further enable radical simplification and a one platform approach. We have already been making good progress in year-on-year reduction of working capital over the last years and with the additional contribution of the “Cash is King”, recently launched “Cash is King” program, we will continue that positive trend and take working capital around 5% of sales for the New Ontex.On CapEx, over the last years up to 2020, Ontex has been spending for 4%, 4.5% to 5% of sales on CapEx. Part of that included a required to catch-up on pants. And Ontex for those of you that remember has been at lower levels before that. In 2021, on CapEx, we have been scrutinizing our CapEx spend, optimizing our CapEx discipline with an enhanced return and return on investment mindset, and grasping opportunities to be more efficient. But also, we've been applying a strict control on spend in view of the margin pressure that we are facing. We are, however, securing all necessary projects to fuel the growth and the saving programs on our North America and Europe businesses, especially in the fast-growing categories of adults and pants. And actually, even in this year 2021, where we expect low CapEx, our CapEx is higher than depreciation when you exclude the IFRS 16 effect on leases. Meaning, that we are on an investment curve and not eating into our future. CapEx forward, the plans are based on the growth and cost-out programs that we have been presenting to you earlier and a range of 4% to 4.5% run rates on the new Ontex is sustainable. I talked about 4% last June, which was covering the total business core and non-core. Capital intensity is somewhat higher in Europe and the US, with more capital-intensive pants and adult inco businesses. But these also have higher profitability that can carry that. The discipline that we display here on working capital and CapEx will lead to a 60% cash conversion for the future, for our new Ontex, returning at the levels that we achieved in 2016.

Next to the balance sheet. Net leverage was 4.3 times at the end of Q3, 3.9 times pro forma if we include the cash from the Brazil litigation that we received early October. And this evolution of leverage has been impacted by a short-term margin pressure. So, deleveraging to a healthier balance sheet is a crucial deliverable for Ontex. And I do want to note a few things on our debt. Over the last few years, our net debt has been slightly reducing and we need to continue to do so. With the refinancing last summer we have diversified our debt with €580 million in bonds and €220 million covenant-holding bank loans. Maturities have been extended to three to five years out. And we do have a solid liquidity with about €200 million of cash and a revolving credit facility of €270 million that we're not utilizing. The execution of our plan, with the divestment of businesses under strategic review will speed up delivery and deleverage drastically, bringing leverage below 3x in 2023, even with a partial divestment and even when making prudent assumptions on divestment proceeds. With full divestments, we should move to below 2x by 2025. This is clearly a very critical milestone in the creation of a healthy balance sheet for our company.

And on that note, let me now hand back to Esther.

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

Thank you, Peter.

So, to conclude, I am confident that the new Ontex is set for success. We now have a clearer strategic direction and this ensures that we can focus our resources and efforts without dispersion. We are bringing down Ontex's structural cost base and addressing the exceptional cost inflation being experienced currently with an intensified savings program, cash discipline, and pricing initiatives. Our mid-term targets remain valid with the new Ontex fully streamlined. With this renewed focus and the greatly reduced structural cost base, Ontex will become leaner, more agile and more profitable. And when the full potential is leveraged, Ontex can generate 15% margins at least and have a debt leverage below 2 times.

Thank you very much. Now, together with the team, we would like, and we would be pleased to answer all your questions.

Q&A

Geoffroy Raskin
Vice President Investors Relations, Ontex Group NV

So, welcome to the Q&A session. As explained, this will be held on the Zoom platform. So, for those who wish to ask questions and are still in the webcast, you will need to connect to the Zoom session through the button that will pop up, or click on the link on the right side of the player. Seen the delay, it's better to mute or shut down the webcast session. Now, if you would like to ask a question, please raise your hand, which you will find in the reaction menu that appears when you hover around with your mouse over the screen. You will all be muted initially. And I will unmute you to raise your question after being announced. Please introduce yourself and limit your questions to two.

The first question comes from Wim Hoste. Wim, I think you need to unmute yourself.

Wim Hoste
Analyst, KBC Securities

Yes. Sorry. Is that better? Do you hear me now? Hello. Do you hear me?

Geoffroy Raskin
Vice President Investors Relations, Ontex Group NV

We can hear you.

Wim Hoste
Analyst, KBC Securities

Okay. Sorry.

Yes, first question would be on the production footprint going forward. Am I right to say that you want to keep, yeah, Mexico as a production hub? But all the other emerging markets would be subject to divestments. Is that how I should read into this?

And then, second question would be on the whole discussion about raw materials inflation and pricing initiatives. I was wondering if you could be a bit more precise about, yeah, current raw material initiatives? What kind of raw material headwind would that mean for 2022? And, yeah, by when should we start to see your selling price initiatives accelerate? And can you put any kind of numbers on how much that could be for 2022?

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

A Good afternoon, Wim. Thank you for your questions. I'm going to take the first one and I will ask Laurent and Peter comment on the second one.

So, on the production footprint, of course, as a consequence of our strategic choices from the geographical perspective, they will have an implication of our footprint. I truly believe that from the European perspective, the footprint that we have in Europe can really fully support the European business. And then, from a North America perspective, we will continue to support the growth in the US and Canada with the production facility that we have in Mexico plus the new facility that we are building and that we are starting as we speak. So, just maybe to put things in perspective, when we think about Mexico, we have two parts there. We have the Mexico domestic business, which is a local-for-local business. It is a branded business, supported by a plant located in Puebla. And then, we have a second plant which is located very close to the West Coast border with the US, which is mostly supporting the US. So, it is early to say how we are going to handle that. But, of course, as we progress with the project of divesting Mexico, we will find the right setup from the manufacturing perspective. But my intention is, of course, to continue to support the US growth with both, Mexico and US production.

Now, on the pricing dynamics, maybe I would like to ask Laurent to mention on the pricing moves. And then there was the raw material for 2022.

Peter Vanneste
Chief Financial Officer, Ontex Group NV

Yeah. Maybe I'll start, and then I'll pass it to Laurent.

Question was about 2022. Can you be more specific? And then, what's the pricing going to be. Let me first start with 2022, and then hand over to Laurent.

We have talked about in my presentation. I've talked about inflation that we're facing a 15% to 20% versus 2020. You will see that coming back in 2022. So what will 2022 look like? We're going to return to growth. We're going to have cost savings and we're going to price for inflation. I mean, those are the dynamics you're going to see. We're accelerating our cost programs to deliver over €80 million and we are in parallel to that, of course, going to be reviewing our strategic portfolio in 2022. You have heard some assumptions already, €80 million will keep our CapEx below 4%. We'll be pricing across the board. And as – although I said, we expect that inflation is going to relax at some point, we do believe that over the next six months, we will at least stay on the levels. And, again, we've not taken any assumption of relaxation in the strategic plan that we've been showing. To be more precise, you know, in 2020 also – it will be year of continued of some volatility. At this point, I cannot be very specific about margins or not as much as you probably would want me to be. We're still in a high volatility. And especially, we are in the middle also of closing agreements with suppliers, closing with customers at this time of year. So, you will understand also that this year, this is more intense and uncertain than in normal years. So, in absence of that visibility, we will come back on that more granularly on 2022 after next year.

And on that, I'll – pricing, specifically, I'll pass to Laurent.

Laurent Nielly
President Europe Division, Ontex Group NV

Yeah. Let me add a bit of a color comments that.

First, I think you will see a different dynamic on the branded business versus our non-branded business or partner branded business. Because, obviously, on the branded business we can price faster, and so you will see pricing entering into actionas - you know - as of now and as of the quarter one right away. On non-branded business, you also will see price moves, but generally takes longer. You also have to remember that on part of our business in Europe, whether it's public tenders or some of the contracts we have, we have fixed price contracts. So, that business takes much longer time to be able to price, because you have to go through a cycle of contract renewal or new tenders. Now that said, we will expect gradually to see the impact hitting our P&L as we progress through the year. And this approach is done customer by customer, depending on the contractual situation that we have and the opportunity that we have. Last, you have to remember that pricing is our main lever, but we have other levers to try to work on value creation with our customers and our partners. On mix, on innovation and on taking cost out, obviously, we have a huge cost program that we have, so it's all about restoring our margin over time, with pricing being the key lever, but not the only one.

I hope it answers your questions.

Geoffroy Raskin
Vice President Investors Relations, Ontex Group NV

Okay. Our next question is from Karel Zoete from Kepler Cheuvreux. Karel, are you ready?

Karel Zoete
Analyst, Kepler Cheuvreux SA (Netherlands)

Yes. Good morning. Thanks for taking the question.

So I've - the first one is with regards to the ambition to have to improve your game in Europe as a private label player and some service levels. Where do we stand today, because you had some issues in Q3? And related to Europe, I think you also had this ambition to raise capacity utilization, but at the same time, you aim to be, yeah, raising prices. So, how does that coincide with each other? And related to that, I think, how frequently is the portfolio tendered?

Now then the other question is on innovation. You speak about a couple of segments where you want to win. How do you judge the competitive strength of Ontex in terms of being able to launch and roll out innovative products? Because ultimately, that also should bring pricing power.

Thank you.

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

Thank you, Karel. I think this is four questions in two.

So, let me – so first of all, you asked about the ambition in Europe, if I understood well, and how that fits with the service level issues that we experienced in Q3. And, of course, we need to make sure that we have best level of service and this serving, especially, the retailer branded business and the institutional business is extremely important. And typically, just to give you a perspective, our target in terms of our level of service is above 98%, which basically means being able to fulfill more than 98% of what our customers need. And that service level has gone down starting from after the summer to the high 80s level. And this is driven by basically material shortage, and especially packaging and transportation. So, we have experienced, especially on the fem care category, where our packaging use significant amount of carton. We've been experiencing challenges to supply the necessary – you know – raw materials. And as a consequence, not being able to serve the customers as we usually do. This is one of the things that has impacted our Q4 outlook. We were assuming that this disruption would go away faster than what we are seeing right now and we are seeing slowly improving the situation, but we are not there yet. And what this means is, we cannot, we need to learn to operate in such a volatile and destructive environment. We need to become more flexible. And we are getting there. So we are slowly improving our level of service and I am sure that, as we go ahead in the year, we will recover and re-establish the required level of service to appropriately serve all our customers in Europe and in the US.

The second question I'm not sure I understood well. That was about capacity and prices of extending capacity while we are increasing prices. And, we are expanding capacity in the product categories that we want to focus. These are faster – fastest growing categories like pants like adult. Most of the growth of the market is basically focused on baby on pants, because the market is transitioning from the traditional diaper to pants. And then, the adult category is growing very fast, because the population is aging and we have more and more consumers getting into that category. And, of course, as a consequence, I mean, we want to have a laser focus on those categories. We want to focus most of our development resources, innovation in those categories. And as we need, we will continue to expand capacity. And this has nothing to do with the price increases. Because, of course, we need to pass a portion of the inflation to consumers and that will translate into to pricing, but we need to remember that, especially in the mature markets, we are selling products that are going to be used anyway to consumers independent in a way of whether there is some inflation or not.

On portfolio tenders, I would like maybe Laurent to...

Laurent Nielly
President Europe Division, Ontex Group NV

I'd be happy to comment. As I said in my presentations, tender is usually every two to three years, but the jury is still out on how it's going to play out in next year. We see both tenders can be reaccelerated if you go into a dispute on your pricing discussions as an example or tenders being extended if the retailers is focusing on first sorting out the service level issues and is afraid of price increase through the retender business. So, I think it can go both ways. But in general, on our contracts, it's two to three years.

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

And then, last but not least, you asked about innovation and how competitive we are on innovation, and I need to say that we – even in – as we have gone through these very challenging periods with huge inflation and unprecedented disruption in the entire supply chain, we have continued to invest in innovation. We have continued to launch innovative products in the market and we have seen very good successes, especially in Europe and North America, but not only with the innovation launches that we've done. As an example of that, the baby pants being redesigned and launched across Europe and North America, but not only also in the emerging markets and new solutions for the healthcare division for the institutions with a smart diaper and all the services that are attached to that.

I hope that we answered all your questions.

Geoffroy Raskin
Vice President Investors Relations, Ontex Group NV

Okay. The next question is from Martin Deboo from Jefferies. Martin, are you ready?

Martin Deboo
Analyst, Jefferies International Ltd.

Yeah. Can you hear me?

Geoffroy Raskin
Vice President Investors Relations, Ontex Group NV

Yes. We can.

Martin Deboo
Analyst, Jefferies International Ltd.

Okay. Good. Thanks.

I want to sort of explore the other leg of the plan, which is the divestments of the non-core businesses. The challenge for you is twofold. You've got to trade those businesses successfully while you still keeping them, and then you've got to realize an exit multiple for them that is sufficient to deleverage the business. So, I guess the questions I want to ask you are, where are those businesses trading now? Maybe the question I can reasonably ask given what you've disclosed, are they EBITDA positive this year? I suspect the answer is, yes, but are they EBIT-positive this year? I'm not so sure about that, because that's going to influence buyer perceptions of value. And do you think you're capable of realizing multiples that will have the effect of delever – clearly, they're going to relieve debt, but are they going to deleverage the net debt to EBITDA ratio? That's the acid test. So I'd just like to hear your views on that.

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

Yeah. So, on where those businesses are today, you know that we don't report specific margins by business. However, when you look at the 2020 margins you have seen that there is a significant difference between the margins that we have realized in Europe and North America versus emerging markets. There is 5 points difference. And as you can imagine, the inflation, the huge inflation and the disruption in the supply is impacting equally the world market. So you could imagine that those margins have suffered pretty much in the same way across the board. Also because, when we look at our cost programs, they are pretty equally spread across the board.

On the proceeding and how we keep those businesses on track while we work on the projects and we look for strategic alternatives, of course, we will have a very strong focus on making sure that we continue to extract and to improve the value extraction of those businesses while we keep them in our portfolio. And, of course, our intention and our target is to rapidly find solutions for those businesses. And as we find them, start divesting them one-by-one. It is too early to talk about expected multiples. I can tell you that we have been pretty conservative in our assumptions when Peter talked about getting our leverage below 3x by 2023 and below 2x by 2025. I can tell you that we have taken the conservative assumptions. And, of course, we will do our best to extract the maximum value for Ontex and for our shareholders.

Geoffroy Raskin
Vice President Investors Relations, Ontex Group NV

Okay. Our next question comes from John Ennis. John, are you ready?

John Ennis
Analyst, Goldman Sachs International

Yeah. Hello. Thank you very much for taking our questions.

So, my first question is on the sort of further cost reductions. I guess, to some degree, the supply chain disruption that you've seen over the second half of this year can be, I guess, to a degree, related to procurement issues and procurement savings have been a historical component within the cost saving plan. So, my question is, how confident are you that the future saving programs won't have an adverse effect on the top line medium-term?

And then, my second question is, I guess, more of a more of a clarification, really, but if you go back to what surprised you for the fourth quarter, is it purely service--related in terms of the supply chain issues that you're referencing or is there also a negative cost surprise embedded within that?

Thank you.

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

Thank you, John. I'm going to ask Vincent to talk about the savings programs and the link or no link to the disruption. And maybe you can talk a little bit about the disruption and what is causing that.

Vincent Crepy
Chief Supply Chain Officer, Ontex Group NV

Thank you.

So, to the question, is our procurement approach having an impact on our capability to have access to material, the short answer is absolutely not. Why? If I will take the example that Esther mentioned, which is packaging material. Fundamentally, packaging material, basically paper-based packaging material and we all are consumers and we order from the big names, et cetera, there's basically shortage of feedstock. So, whatever approach we can have on procurement with our direct suppliers, they themselves do not have access to the feedstock, which in repercussion translates in problem of availability. Now, going forward, procurement-wise, what we plan to do is have a diverse asset base qualified in order to increase the resilience of our supply chain going forward. But, again, when the feedstock itself is not available, this is a common issue across the board, not only for Ontex, but for anyone using those feedstocks. So, that's on the procurement savings having or not having an impact on the disruption. And the answer is, absolutely not.

Now, on – the question was about service. I'm not sure I got the question actually.

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

So, maybe just to close on the disruption, because we've been spending a lot of time on this disruption. I do believe that this is of a temporary in nature. And, of course, we need to make sure that we do everything to make – to compensate and do everything in our hands to offset. As I said, be more flexible, qualifying new suppliers. But there is, if there is a shortage of a specific source of material there is little that we can do. And, I think that is a combination of, things step-by-step getting back to normal from the supply/demand perspective. And us getting better at operating in this extremely volatile environment, and we are getting there and we are doing, different changes together.

Now on the service level, the question, I think it was more on in Q4 the surprises that we had were they only service related? I would say mostly, yes. We were expecting that, even if we had a prudent assumption, we were expecting to recover our service levels much faster than what has happened in Q4. And that has impacted, both top line and margins as a consequence.

Okay. So, next question.

John Ennis
Analyst, Goldman Sachs International

Thank you.

Geoffroy Raskin
Vice President Investors Relations, Ontex Group NV

Okay. Next question is from Nick is from Nick Roope from Barings. Nick, are you ready?

Nick Roope
Analyst, Barings

Hey, guys. Can you hear me okay?

Geoffroy Raskin
Vice President Investors Relations, Ontex Group NV

Yes, we can.

Nick Roope
Analyst, Barings

Thanks. And thanks for the call and the presentation.

My first question is, given your 2023 margin guidance is based on disposals, should we expect that to change based on how successful or unsuccessful you are on disposing of the low margin parts of the business?

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

You want to … So, basically, the question is, if we are not successful to this. So basically, first of all, the margins are assuming partial disposals and we are having conservative assumptions. So, we are counting on growth on the continuous cost effort with the 4% productivity year-over-year. And I need to say that, we are assuming the level of raw material prices as they are today, which is highest level ever. So of course, you will need to look at all the variables. So we are focusing, first of all, on committing to what we can control, which is going back to growth at least 2% to 3% growth, getting a 4% productivity year-over-year and making sure that we have a laser focus on cash and the CapEx and cash. And then, there are some variables that we cannot control, which is, raw material prices. We are taking a very conservative assumption at this point, which is they will stay at the level they are today. While my expectation would be that at a certain point, we will see some softening of that. And we are assuming, that step-by-step, we will divest the different businesses with the conservative assumptions also on the proceedings, but maybe Peter, can....

Peter Vanneste
Chief Financial Officer, Ontex Group NV

Maybe one thing to add. You did hear well. I presented the assumption that we fully divest by 2023 to get fully in all the KPIs that we presented. If that doesn't happen, we also get there without any divestment, if there is a 5% relief on the inflation. I've talked about 20% increase of inflation. That's how you have to benchmark it. With the 5% release, we also get completely in that guidance without any divestment, which again is not the game plan, but that's the sensitivity around that.

Nick Roope
Analyst, Barings

Okay. That's clear. So just, so the graph on page 5 is all or I mean I know it 40% to 80% but you've had roughly 20% increases in your input costs in 2021. If that reversed 5%, you're saying, so about a quarter of it came back, you would just get there for free so to speak. Is that what you're saying?

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

Yeah.

Peter Vanneste
Chief Financial Officer, Ontex Group NV

Exactly. It basically means we're doing our work on the cost saving programs to offset a lot of it and then on top of that, we will have pricing that will cover the gap.

Nick Roope
Analyst, Barings

Okay. But currently the 13% is based on flat raw materials and fully doing your disposal program?

Peter Vanneste
Chief Financial Officer, Ontex Group NV

The numbers you've seen in the whole presentation is assuming no relief on that peak level inflation.

Nick Roope
Analyst, Barings

Okay. Got it. That's clear. And then sorry, a slightly precise question, what's the last data point on slide 5? Is it Q3 2021?

Peter Vanneste
Chief Financial Officer, Ontex Group NV

Slide 5...

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

Slide 5.

Peter Vanneste
Chief Financial Officer, Ontex Group NV

Can you refer...

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

Can you refer, you know, what...

Peter Vanneste
Chief Financial Officer, Ontex Group NV

slide 5?

Nick Roope
Analyst, Barings

It's the raw material price file. I'm just – I'm basically curious what the latest data point is and how much forward looking? I don't have these precise indices myself. I'm just curious what you think – I know you mentioned, they're going to be about flat for the next six months. I'm just curious whether you mean Q4 and Q1 or Q1 and Q2?

Geoffroy Raskin
Vice President Investors Relations, Ontex Group NV

The last data point is end of this year.

Nick Roope
Analyst, Barings

Okay. So you already have Q4 2021 on the slide 5?

Geoffroy Raskin
Vice President Investors Relations, Ontex Group NV

Based on our own estimates, yes.

Nick Roope
Analyst, Barings

Okay. Got it. And so then you're saying that prices are going to be – so your six-month comment was for the first half of next year on raw materials?

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

Yeah. We are assuming raw materials, so we have seen the highest peak of those indexes in Q4 and that's the last figure, the last data point that you see in that graph. And we are assuming that that level will stay throughout the entire 2022 and 2023. And what we are saying is that, we – and at the same time, we are targeting the divestments. So, if only we saw softening of those – that peak by 5%, which is as you said, a quarter of the increase that we've seen throughout 2021, we will get to our 2023 targets without any divestiture. Or we are divesting the businesses that are margin dilutive to the overall company. With that level of inflation staying fixed for the next two years, we can also get there with all the cost programs that we are targeting, the 4% productivity that we have talked about. And probably the final outcome is not going to be one or the other. And of course, if we – as we drive the divestitures and raw materials soften, I think there is an opportunity. And that's why we say that – and I say that I see this business with the potential to grow beyond the 15% EBITDA margins because the level of raw material prices that we see today I don't believe will be the case in the future. We'll continue to drive cost productivity and we will basically focus on the most profitable business driving growth and mix in the profitable businesses.

Peter Vanneste
Chief Financial Officer, Ontex Group NV

And maybe just to...

Nick Roope
Analyst, Barings

All right. Got it.

Peter Vanneste
Chief Financial Officer, Ontex Group NV

...as we talked...

Nick Roope
Analyst, Barings

Sorry. Go ahead.

Peter Vanneste
Chief Financial Officer, Ontex Group NV

We talked about relief on the cost. I do want to reemphasize we're not counting on it. Our full plan is based on that we are on this peak level. And if I – if we talk to Vincent about cost or Laurent about pricing, this is the challenge that we are looking at. That's the current level of inflation. We're not assuming any relief in what we do.

Nick Roope
Analyst, Barings

Yeah. That's really clear. So, I know it's my third question, but just to be clear, when you were commenting that you kind of expect them to be flat over the next six months, is that based on conversations with your suppliers or is that just your own expectation?

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

It is our own expectation. I mean, I don't think anybody has the crystal ball and many people have proven to be wrong on assumptions. We know what the prices are today and we know that some of these prices will impact Q1 because typically when the indexes move, there is kind of a three-month – one- to three-month time lag between when the index move up or down and when you see that reflected in your price. So, this is what we see today and we are assuming that they will stay, but it is very difficult to predict what is going to happen next year.

Nick Roope
Analyst, Barings

Okay. Thanks for taking all the questions, guys. That's really clear.

Geoffroy Raskin
Vice President Investors Relations, Ontex Group NV

Yeah. That were about 10 questions, John. Anyway, the next on the line is Eric Wilmer. Eric, are you ready to bring your question?

Eric Wilmer
Analyst, ABN-AMRO ODDO BHF BV

Yes. Thank you very much. Eric Wilmer, ABN-ODDO.

I had a question on your European core business. I would like to dive a bit deeper in that and more specifically on sustainability, innovations, and online. In terms of sustainability, I think many of your clients have committed themselves to very strict greenhouse gas emission reductions, where private label, especially for disposable hygiene products can be a very effective tool, especially if they tender it to the cleanest company out there, the cleanest manufacturer. For this, you will probably need to use fully recycled raw materials in your products and make your product itself also fully recyclable, use no virgin plastic, et cetera, et cetera. I think that it's fair to conclude that several of your peers both branded and non-branded are quite a bit ahead in this. So, I was wondering could you shed some lights on your game plan when Europe again becomes the core focus. So, probably talking about 2023.

And what is your strategy concerning online, especially in online channels where there is no private label and where basically the A-brands are mainly benefiting from the increased trend to online? Thank you.

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

Thank you, Eric. I'm going to ask Laurent to answer both questions.

Laurent Nielly
President Europe Division, Ontex Group NV

Two core questions on future proofing our business, isn't it?

And on sustainability, I think that – a couple of points. You're absolutely right that we see increased level of requests from our partners to – for us to help them achieve some of their sustainability goals. And for us, as an actor in the society to raise the bar. Recycled material is one of them. Reducing our carbon footprint and especially looking at Scope 3 over time but how we measure it is something that's important, that requires that we're going to have to partner with all our partners upstream and downstream. And also using less material where we can. So, we're looking at all of those elements. You've mentioned that some of our competitors might be ahead. I think it depends on the solution that you look at. For instance, on packaging, the greatest way you can have impact is to increase the amount of recycled PET that – PE that you're going to use in a lot of your materials and not just going into paper bag, if it's that you were assuming. But we're working all those assumptions. It is fair to say with the current crisis on supply on a lot of those materials, and you can imagine that every kind of eco-labeled supply is even more hit with imbalance between demand and forecast, we have a bit of delay on rolling some of those initiatives. So, you're absolutely right that you should expect more focus on it on the second half of 2022 and going into 2023 when the situation is more stabilized.

On online, I don't think it's accurate to say that private labels are not online. I think if they are not on some of the big marketplaces like Amazon, although Amazon has a private label program of its own, but we are very present through the websites of our retailers and we are helping them to perform better on the way they position their brands on the basics about growing online. So, this is something that is really core to what we do and on which we have, your right, a lower share than some of the branded players, but it's growing nicely. And then, we know that it will continue to grow, but probably never reach the full impact of a branded player until all our partners invest in their own infrastructure. So, that's how we're growing through it.

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

And maybe to finish on online, apart from helping our customers to gain their fair share online and going directly to some of the customers with retailer brands or their own brand solutions, we also are the partner of choice of most or many of the lifestyle brands. I mentioned before, these are brands that appeal to younger, maybe, generations with good for you, good for the environment type of promise. These are kind of premium products, typically priced higher than average, with a promise of natural materials, sustainable materials. And a big portion of the sales that these brands have are online. And we have a very, very strong presence and penetration on that segment.

Geoffroy Raskin
Vice President Investors Relations, Ontex Group NV

Okay. The next question is from Mohammed Ishtiaq. Please present yourself and ask your question.

Mohammed Ishtiaq

Hi. Thank you very much for taking my question. I have three.

Perhaps we can start with a more high level question which is looking at the business historically, it's generated kind of 10% to 11% EBITDA margin. And now you're saying that through the price increases that you are pushing through in a very elevated raw material input environment, you think you can still reach 13.5% – you know, 12% to 13.5% EBITDA margin, if those prices increase – decrease by around 5%. So, I guess, what I'm trying to understand from your perspective is what's changed between the last couple of years where you were a 10% to 11% business versus what's going to change in 2023? If we don't assume any of the disposals take place and you just have a 5% reduction, is it simply that you have been mispricing your product over the last couple of years? And now, you think that the pricing will let you achieve that [indiscernible], or is there a fundamental shift in business that we also need to take into account? That's the first question.

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

I'm not sure if I understand the question. So, can you repeat it? So, you say, historically we had 10% to 11% EBITDA margins. We are promising by 2023 12.5% to 13.5%, with an assumption of raw materials softening 5%, so a fourth of the increase that we've seen in 2021. So, is the question – could you repeat the question, so the framework is clear?

Mohammed Ishtiaq

Yeah. And so the question is what's changed between when you were 10% to 11% business versus 2023? Is it simply that you're just increasing prices on your product portfolio, or is there a fundamental shift in the business? Basically, how can we get comfortable with you achieving that margin when your historical performance hasn't been there?

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

Okay. Okay. So first of all, our – the cost has gone up. So assuming the 5% softening, so it's still a 15% cost increase. In the meantime, we will have had four years – three years, 2021, 2022, 2023 of around €75 million of cost savings. And then of course, we are focusing on the margin accretive categories. So we have been working, especially this year and for the years to come on addressing the low, profitable products subcategories. And in fact, when we talked about granular approach to price increase is, of course, customer by customer, but we are looking also at SKU by SKU to make sure that we address the low profitable SKUs. Also, because the inflation – the starting point was not even and the inflation has hit differently the different product segments. So, as a summary, big inflation, but also a very aggressive cost programs and the radical reduction of complexity independent on the divestments, which – because all those businesses are kind of local-for-local. Did – the work that we've been doing this year is to radically simplify our organization and the way we operate to impact also the SG&A. SG&A will play also a key role. As you know, over the years, SG&A went up, almost up to 13%. We've done a big step this year, bringing it down almost 2 points. And we will continue doing so. As Peter said, my ambition and my target is to get SG&A down to below 10%. So, it's going to be a combination of SG&A reduction, product efficiencies to compensate the inflation, and pricing to make sure that we address the low profitable segments. And this is independent on the divestitures. This is to make our core more profitable.

Mohammed Ishtiaq

Understood. That's very helpful. Thank you very much. So, staying on this point around the simplification of the product portfolio and the simplification of the process, I guess one thing that Vincent was very helpful in kind of explaining was how you were going to perhaps redesign the production process for some of your products. Is there a risk that as you move to try to simplify the production process and try to bring everything on one platform that you may risk your efficiency levels from – or your volume targets from 98% because there is some level of malfunction or some level of any movement towards more simplified process?

And also, are you – you mentioned that you're seeing inability or – sorry, unavailability of some raw materials in your current production. Does that mean that you have to ration amongst the businesses, i.e.

when you do get, for example, cardboard come through, does that – are you making sure that that's more available to the private label business versus the branded business where you have a higher margin because you have certain volume commitments that you have to meet? How are you managing your raw materials amongst the various businesses?

Vincent Crepy
Chief Supply Chain Officer, Ontex Group NV

So, I'm hearing two different type of – two blocks of questions. One around harmonization and having one platform, is that going to deteriorate our capability to respond to consumer needs. So this is one block. The second one, the second block I'm hearing in your question is around the day-to-day allocation of product on this type of things. So I hope I got it right.

So, on the first one. Harmonizing across categories, plants and equipment actually is going to help us to react and to be better adapted to consumer needs. Simplification and harmonization doesn't mean eliminating completely some level of adaptation to the local needs of a given customer. Quite the opposite, we want to harmonize on some key elements to unlock capacity and capability and add features that we can then apply if you wish in a rigorous manner locally, so that we serve specific customers. So I don't see our approach to harmonize, to simplify, to build on less platforms, faster equipment is going to be detrimental to our capability to serve customers. I mean, actually quite the opposite.

Now, the second question around the way we manage the situation when there is a lack of materials. So, a couple of food for thought. First is this extreme volatility unexpected, the lack of this and that and the rest of it is just a reality that is across the board. How we can react to that is basically doing two things to increase our resilience. First is get better visibility so that we can anticipate faster or better at least. So that means, for instance, tracking containers, understanding where the supplier is so that we can anticipate if there is a delay. The second thing is – first visibility. Second is flexibility in adapting to the change that we can see a little bit earlier. So this could be, for instance, developing the capability to ship. We took the example of – you took the example of outer case. If there are some SKUs that we can ship without outer case, agreeing with the customer, we will do that. So, this combination of anticipation and better reaction will help us to actually manage. Now, if at the end of the day, we have to make a choice between an SKU and another, that's the type of things that we want to avoid doing, actually. But if we have to do that, we do that in collaboration with the customers.

Mohammed Ishtiaq

Understood. That's very helpful. And just my final question is the €130 million of one-off costs associated with the cost savings program. How is that going to be funded? Is that a P&L cash cost every year or is that funded partly through your CapEx program of 4% of sales per annum?

Peter Vanneste
Chief Financial Officer, Ontex Group NV

It’s P&L funded, not within the CapEx. And, again you talked about the €130 million, that's the cash indeed. That's on the P&L.

Mohammed Ishtiaq

Perfect. Thank you very much.

Geoffroy Raskin
Vice President Investors Relations, Ontex Group NV

Okay. Our last question today comes from Anna Murray.

Anna, please introduce yourself and limit yourself, please, to two questions.

Anna, are you there?

So that will be the last question then. I pass over to Esther to wrap up then.

Esther Fatima Berrozpe Galindo
Chief Executive Officer, Ontex Group NV

So, thank you so much for your questions. We will deliver on the turnaround of Ontex. Thanks to all the efforts to improve performance in the areas where we have full control. The benefits will become more visible once the unprecedented headwinds soften, which I am sure they will at one time. In two or three years from now, I am confident that this new Ontex will be very different from today, delivering a solid financial performance and creative value for our shareholders. Thank you. I hope you stay safe. And I take the opportunity to wish all the best for the new year to you all. Thank you.