Thule Group

Thule Group Interim Report Q1 2019

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Results Overview

Magnus Welander

CEO, Thule Group

Welcome

Good morning, ladies and gentlemen, and happy to have you listening in to our quarter one 2019 report call. It is always good to start the year in a good way, which is exactly what we have done with 2019.

Promising start to the year

So if we go to the first slide of the presentation, you will see that we started the year with a net sales of SEK 1,834 million, which was then a growth of 13.8%. In a currency-adjusted growth, that was 7.5%, and as we did the acquisition of the small company, Tepui, late last year in December, we also got some growth contribution from that in quarter one. The true organic constant currency growth rate was 6.4% for the quarter.

As we had planned and communicated, it was the region Europe and Rest of World that was in the driving seat and grew 10.3%, currency adjusted, while region Americas declined with 0.7%. I am going to comment more about the regions later on. The development was in line in our expectations, so in line with what we thought.

In terms of EBIT, we reported an EBIT of 18.7% EBIT margin and SEK 342 million, which was also in line with our expectations and according to the plans.

So, totally, a solid start to the year in terms of all aspects, and we are off well for the peak season that is coming in.

Net sales and EBIT development

If we go to slide 3 in the presentation you will see a little bit more on the financials. If you look at that slide, it states the growth, as we once again said, of 13.8% on sales, 7.5% in constant currency and 6.4% in constant currency organic growth.

I think it is interesting to look at the EBIT margin, because obviously you see a small drop from 19.2% EBIT margin to 18.7%. You should remember that, if you would look at last year's EBIT margin in constant currency, it would be instead 18.9% comparative. That therefore means a 200-basis-point drop, which was in line with our expectations.

So, a solid start for the year, with numbers in what we thought.

Region Americas

If we go to slide 4 in the presentation, which is the presentation about Region Americas, we can say that it started slow in the beginning of the year, as we expected it would. There were several reasons, as we have communicated previously with our plans to phase out some business, plus some expected tariff impact in some delays.

But if we go through it well, let us start with the small acquisition of Tepui. This acquisition has really been quickly and well implemented in our business, and everything is up and running as it should, so we are very happy to say that that has been quick and smooth. Their sales in the first quarter for their rooftop tent products was SEK 18 million, which is also a growth in true organic growth versus what Tepui sold in the same quarter last year, so a positive development.

We have communicated a long time that we are expecting to see the drop of our OE products that we are phasing ourselves out, which is both some accessories to pickup trucks, as well as two bag and case collections to leave. In fact, the decline was a lot less than we thought in quarter one, so some of that decline effect will instead hit the coming quarters comparatively. It will still, by the end of the year, be the expected SEK 45 million that we have communicated in total decline this year. So we have SEK 45 million as a total, but it was a little bit less decline in this quarter.

If you look at the other parts that impacted the quarter, in the US we have a strong channel in the independent bike dealer channel. We historically have a strong spring with those guys selling a lot of our bike racks. We still expect, also, 2019 to have a very strong spring, and we see good numbers also here in April already we can say, but normally we would have had some preseason orders at the later part of quarter one. This year, however, those independent bike dealers expected an additional tariff to hit on 1st January 2019, which was previously communicated. So we had the first tariff impact on Chinese imports in September 2018 with 10%, and then a previously communicated additional 15% to hit as of 1st January. What then a lot of the independent bike dealers did, since they buy most of their bikes from China and 15% on a bike is very much money, is they decided to buy a lot of bikes at the very end of quarter four last year. Then the tariff was postponed in a communication by the US authorities, first communicated as a 60-day postponement, and then an additional postponement. Now nobody really is sure if it will come or not, this additional 15%, but it means that a lot of the small independent bike dealers tied up a lot of cash with expensive bikes. Since we have a very strong track record of on-time improved delivery performance and we have local manufacturing, that meant that we saw fewer preseason orders than we normally do, and therefore we are feeling very good that we will see some of that pick up, as already I mentioned starting to see it in April, do the same as the season goes.

Secondly, we also saw that for the first quarter in a very long time we did not have growth in Canada; we had a slight decline. That was very much due to a phasing versus last year where, at the very end of quarter one, we had some big load-ins to two big retailers in Canada. We are very calm about our continued total growth rate in Canada being similar to the last few years, where Canada has been the strong performer in North America, so no worries whatsoever in terms of total performance.

Thirdly, we have some challenges in the overall economic situation in some of our mid-sized Latin American countries like Costa Rica, Colombia, Argentina and Panama. That is a reality of a tougher economy there, but we are doing well in the biggest market, Brazil, so we are still positive overall for Latin America.

If you look at the commercial launches, the key launches for the period, this was really the first big quarter for the US organisation and the North American organisation for the new roof rack generation. That has been very well received in the market and is rolling out well. Then, in this region, as well as in Europe and the rest of the world, we hit the market with our first hard case luggage collection ever, the Thule Revolve. That has been very well received in the market. Also, in terms of Thule Sleek, the four-wheeled stroller, which was launched later in the year as we initially, last year, focused mostly on Europe, it is starting to get really good listing in various department stores and juvenile stores. The listings part is rolling out well; we now need to see during the rest of the year in terms of the true sell-out in the North American markets.

Region Europe and Rest of World

If we turn to the next slide and look at the strong performance of Europe and Rest of the World, where we had a 10.3% constant currency growth, you can say that in general we had a very strong start to our Sport and Cargo Carriers. Part of that is a phasing situation a little bit the other way around than we just mentioned in the US. When we talk about our bike racks, which is our biggest category in Sport and Cargo Carriers in Europe, we have mentioned many years that we are a little bit dependent on how quickly the spring season comes, not in total sales over the year but in whether some of those sales come late Q1 or early Q2. This year, the second half of March had some great weather. Spring weather was tempting for a lot of consumers, and we had a very strong start of the season a few weeks earlier, actually, than we had in 2018. So we are very confident over the bike rack category's total growth, but it was a little bit exceptionally strong at the very end of Q1 as well. So a little bit of phasing effect, but generally, aside from that, a very strong performance in Sport and Cargo Carriers.

Also in Packs, Bags and Luggage, a solid start with nice growth and the big growth driver being the Thule Revolve hard case luggage launch, which is going as well as we planned, which is very nice to see. Production in Poland is running well, and we are getting very good orders. And early to tell, as often is the case, so early in the year how well it will sell through, but, in terms of orders from retailers, listings, a very solid start. Also, the Thule Revolve has helped to create momentum in the Thule Subterra soft luggage, a little bit what we internally have joked about saying: it is difficult to win when you have an army of one in a store. In some stores we have only had the Thule Subterra luggage, therefore maybe not the impressive presence that you would want as a brand. When you now add, in the same stores, a hard case collection as well, we start to become more of a brand in the stores, and that has actually also helped our Thule Subterra luggage.

And then, in this region, as we know, similar to the US but with less impact, we also see a shrinking legacy product category, but that is becoming smaller. It is shrinking a little bit less in quarter one than we did last year.

In the Active with Kids category, we continue to grow at a very fast pace. The multisport/bike trailers category is doing great, going very well for us. Child bike seats is chugging along very nicely, and we continue to grow in our Thule Sleek rollout in the stores. So we are seeing good communication and good throughput there.

Finally, in this region, we do sell a lot of products to the RV market: awnings, bike carriers and a few other things. We have communicated for quite some time that we believe there is an adjustment necessary in the market. That adjustment is happening a little bit, but it is coming a little bit later than we thought initially, so it was actually a relatively okay quarter one, with less impact than we thought from the market perspective. We are doing very well, outpacing the market significantly. We had a very strong start for RV products, stronger than actually expected, with a market that is flattish in terms of registrations if you take all over Europe but where the core markets for Thule Group, which are the German market and the central markets in Europe, doing better than the Nordics and the Brexit-exposed UK. So we are in a slightly better situation than we expected. We still expect the market to be slightly cooler for the full year but feel very confident about our growth ability in RV products as well.

I then leave it to Lennart to talk a little bit more about some of the other financial numbers.

Financial Results

Lennart Mauritzson

CFO, Thule Group

Reported income statement

Thank you very much, Magnus. So we are at slide 6, the income statement, now.

Gross margins were down in the first quarter versus the prior year 0.9 percentage points, including an unfavourable currency effect of 0.4 percentage points. There was a decrease in gross margins, in constant currency, then, of 0.5 points, driven by the negative materials price development we had communicated that we will see in the beginning of this year, at least, year over year. This was not yet fully compensated by our ordinary customer price increases that we do implement in the first quarter. There was also the fact that the Chinese tariffs on US purchases implemented during the autumn with the first 10%, where we only do a like-for-like price increase to our customers, hit our gross margins as well.

Our selling expenses are higher than prior year in absolute numbers. In percentage of sales, we ended the quarter at 17.8% versus prior year 17.6%, due to the product development push and commercial initiatives, primarily in our new categories.

The financial net was minus SEK 13 million in the quarter, versus minus SEK 16 million last year. This year we had no unfavourable currency impact, while prior year we had minus SEK 5 million impact. External borrowing costs were slightly lower than prior year, and this year we also have a negative effect by the new IFRS 16 accounting rules, implemented from 1st January, with SEK 2 million extra in our financial expenses due to that. However, you can see on the right-hand side of the page that we had very little effect on our income statement due to the IFRS 16 change. So we have a favourable impact of SEK 1 million on EBIT in the quarter and a negative SEK 1 million on the net income. Effective tax rate for Q1 was 23%.

Operating working capital and operational cash flow

If we turn to slide 7, the operating working capital and operational cash flow, this quarter we ended with SEK 1.6 billion in total operating working capital, which is 24% of sales versus the 21.4% prior year. As communicated last report, increased levels of special inventory is in line with our expectations and plans, and we do not expect the inventory levels to go back to more normal levels until the second half of this year, after the peak season is done for our biggest categories. Therefore it follows the pattern for the operational cash flow, with the build-up of working capital preparing for the coming sales in the much larger sales Q2. We had a negative operational cash flow by SEK 75 million, versus prior year minus SEK 69 million, but we will see significant improvements in Q2 and Q3 following.

Thank you very much.

Outlook

Magnus Welander

CEO, Thule Group

Performance versus financial targets

Thank you, Lennart. So, overall, if you look at slide 8 and our performance versus financial targets, we feel very good that we are tracking to our plans with a solid organic constant currency growth, boosted with the small acquisition of Tepui in total growth. We are tracking to what we expected in terms of our EBIT margin, and we see that we are, with the new rules of IFRS 16, at 1.9x net debt to EBITDA leverage, while if we would exclude the IFRS rule, it would be 1.7, comparable to what we have presented historically.

There is an annual general meeting today where the proposal of a dividend of SEK 7 per share is being presented, and that would mean a net 86% dividend to net income.

Focus areas for the coming months

If we turn to the future, on this last page, for the coming months on what we focus on, on page 9, first of all it is great to sit with great products and a production setup that is working very well. We have done major projects in all six out of the nine plants without any disruptions, we have shifted our Western European distribution centre without any disruption, and we expanded our Eastern European distribution centre without any disruption to our business. That means we sit with full inventory levels, we have some great new product launches and we have a good performance in our plants, which makes me very confident ahead of the peak season.

In terms of sales and marketing, a lot of focus is going on, of course, as you would imagine, truly both establishing ourselves and also driving sales through in our two additional focus categories, so to speak, the new ones of luggage and strollers. That has of course meant that we have hired some new people in the bigger markets, where it merits own dedicated sales forces – generally, key people from the industry with good experience to be added to our own internal competencies. It also means that we are doing a lot of initiatives at various smaller personal events locally, especially in juvenile, and we think that these are keys to drive the long-term growth.

In terms of product development, we are running a number of parallel big projects. We have just started sales on a number of very recent product introductions but, more importantly, the annual fairs are coming earlier and earlier every season, so many of the fairs that historically would have been at the later end of Q3 are now even at the very beginning of Q3, or some of them even at the very end of Q2, in June. This means that our product development efforts are pushing very hard to be ready with all those new products that we will be showing retailers in June, July and August for then launching them to consumers in 2020. We feel very good about all our projects, some very exciting products to come, and we have decided to continue at the high development spend level, which is around 6% of sales.

Then, finally, in an operational way, it is of course a huge peak season for us in that we are at the very moment with the most people that we will have any time during the year in our plants. We are running several shifts in most of our plants; it is a very exciting peak period. In that peak period there is of course also a focus, having done a number of major investments in our plants in 2018, we are starting to see what is a big focus, which is to capture some of those efficiencies that those big investments and layout changes to the plants should deliver on.

Then we are in the finalisation stages, especially in our US site in Seymour, where we have constructed an additional building with a fabrication plant next to our assembly plant, where we are in the midst of the last phases of that, which will be ready in May. We also needed to expand our Belgium RV products site after those years of fantastic volume growth, and we have, therefore, also the last phases of that start-up of that additional small plant.

Then, finally, we are in phase two of our big roof rack generation rollout, which means that the Swedish plant is still going through some major innovation in terms of assembly lines. However, we feel very good on the performance, and I have to say that the operations team in the company and the supply team has done a tremendous job to run so many plants, so many major projects, without any issues in terms of disruption of deliveries. So, a fantastic job of that team.

With that, I leave the floor open for questions.

Q&A

Daniel Schmidt (Danske Bank): Hello. Good morning, Magnus and Lennart, I hope you can hear me. Just a first question, a couple of subjects, to start with. With RV and what you said, you sounded like you were outgrowing the market quite a bit, and you also said that you were a bit surprised about the fact that the slowdown in the market implicitly sounded like it was less than you expected. Would you say that the start of Q2 has been a bit more like you were seeing at the start of the year? What is the trend currently in RV when it comes to production? I think that was that one.

Magnus Welander: Yeah, morning, Daniel. Yeah, I think, if you look at it, we see a trend. We thought the RV manufacturers would have gone more aggressive, like they have done historically sometimes in the past: extending Christmas holiday breaks, not getting so many back, when they were now doing this pipeline adjustment. So more of a stop-and-go type of thing, and then be calmer in Q2, Q3. But it seems more like they have done a more balanced way, which is actually better for everybody, I think, and are not taking a big hit, so to speak, in Q1 but rather balancing it out, spreading it thinner.

So it is not like there is a dramatic change in our expectations for Q2. It is more that it will be more slightly slower the whole time. We were more fearing a very aggressive turning off the switch almost completely for a period in Q1; they did not.

Daniel Schmidt: Right. But is it fair, then, to say that this inventory correction will be going on a bit longer than you expected at the start of the year, or are you seeing retail demand in your markets improving going into Q2 and sort of taking the edge off the need to destock?

Magnus Welander: I think the need to destock is there. We are not changing our opinion on that. What we are seeing is less of a step quarterly effect than we maybe thought, and it is going to be more consistent. We have not changed our mind on what we believe, roughly, that destocking is. But actually Nordics is a very specific market. UK is a specific market due to other reasons: UK due to the Brexit, Nordics due to some of those emission rules. But if you look at the big markets, Germany is doing well in registrations. Some of the other central markets are doing really well in registrations. If you look at Trigano's recent report, if you look at some of those caravan statistics, it is not doing that badly. It is tainted a bit by the Nordics and the UK, luckily not our most key markets for our products; we are more central Europe. Overall, it is roughly in line with our expectations as a total, but it more smoothens out.

Daniel Schmidt: Okay, good. Then, just very briefly, on the portfolio pruning, the remaining SEK 33 million; is that going to be done in Q2 or is that slipping into Q3 as well?

Magnus Welander: You are right. Our expectation now is that that now will actually slip in, spread out also longer. It is the same amount, but it will probably spread out longer into the second half as well. We see it is unlikely that it will all happen now in Q2. It probably will be spread over the whole year.

Daniel Schmidt: Then, thirdly, raw material was negative; it was a headwind for you in Q1. Is it fair to believe that raw material will turn, gradually, to be a tailwind by the end of Q2?

Magnus Welander: It is definitely going in the right direction. Tailwind is always a questionable thing. It will be less negative, initially, we know that much. And it will go in the right direction, if you compare it then of course with the price increases implemented as well, so you have to do both for the comparisons, so to speak. But yes, it is improving in the right direction.

Daniel Schmidt: Then the last one, for modelling: you said you are pushing product development very hard right now and some of the plans have been brought forward compared to historical dates. Are you implicitly saying that Q2 will be more heavily burdened by product development spending, but the overall figure is going to be 6%?

Magnus Welander: No. The reason is, mostly at the fairs we will be showing very professionally made but still prototypes, which is not the heaviest impact cost when you do things. You have various things impacting your product number, so it is going to be spread very similarly to previous years. It is more of a time pressure, let us put it like this.

Daniel Schmidt: Right, okay.

Magnus Welander: If you look at it this year, the guys have had a little bit shorter time than normally between the previous year's launches to get them ready and to show them to retail, but, from a cost perspective, no.

Daniel Schmidt: Okay, thanks. Thank you.

Peter Reilly (Jeffries): Good morning, gentlemen. Can we talk a bit about what is happening with Packs, Bags and Luggage? You say in the release that it grew in Europe; I guess it is still shrinking in the US because you have the bigger impact from legacy products being phased out but, overall, did PB&L grow in Q1? Are you on track to grow for the full year? In particular, can you talk about whether the Revolve had any significant impact or whether it is just all very small numbers currently, because it is the initial stock orders. So maybe you can help us understand what is happening with PB&L, please?

Magnus Welander: Yeah. We actually were flat in the US, so that means, since we grew nicely in Europe and the Rest of World, we had a growth in Packs, Bags and Luggage, not a big growth but we had a growth. We are still being pulled down in region Americas, as you mentioned, by having a significantly larger share of those legacy things, but overall that is, of course, shrinking as we go. Even in Americas, where it is a much bigger share of the total business, with more old case luggage stuff, it is dipping fast there as well. So that is good. The key contributor for that was Thule Revolve and some of those what we call everyday backpacks, so the Thule backpacks that you would use to work or to go to school with, university with. Those are the two strong performers, but actually we are doing really nicely also in the small, niche categories of tech packs and sport-specific bags. So, overall, I think a promising first quarter. Volumes are not huge in Thule Revolve in quarter one because we only started selling it as of February, mid-February, right, so you have only had 1.5 months. Impact will be more positive in Q2 and going forward, which will evolve in terms of volumes.

Peter Reilly: Also, in terms of mix, obviously you had a small mountain to climb in the first quarter for reasons you talked about, but should mix still be getting better as the year progresses, because you will have the legacy products phasing out? Hopefully you have got rising contributions from newer, higher-margin products? Do you feel confident that you should have a steadily improving mix as the year progresses?

Magnus Welander: Yeah, we have absolutely in our plan a mix improvement, as you mentioned, for these reasons. What we have also made clear is that, versus last year, we do have a tariff impact on the gross margin. So, indicatively, the tariff in itself, since we just decided to pass on the exact cost increase, not with a mark-up on it, on the tariffs, that means, if you take that effect, that was about a 200-basis-point effect in quarter one, just from passing on only the cost increase. So if you take away the FX-adjusted part of what happened to our EBIT line and you take away that margin impact of only passing on the cost, actually the rest of the mix was flat in Q1. That means, by default, as you mentioned, less of legacy, less of OE, some better products; yes, we should see it positively develop.

Peter Reilly: Then, lastly, you may not want to answer this, but can you give us any hints about the new products that are coming later in the year? Obviously you will not want to talk about the details but, in terms of the scale and importance, are these minor infills or are these relatively major launches that will create a meaningful impact in years to come?

Magnus Welander: So, if you look at it, in the classical category Sport and Cargo Carriers, we have launched the big things just end of Q1. They are going to have their big numbers in Q2, Q3 due to the fact that that is when people buy those products and there is generally, as always, some very good new bike carriers. We are coming this autumn with an additional thing what we have already communicated - a new top-of-line roof box which is only coming in the second half of the year, the Thule Vector. Even if the most premium roof box is not the one that creates the biggest volume, that will be, of course, a meaningful impact in the second half of the year with a new premium roof box.

Then, in the categories where we truly see some products that will generate, if we are as successful as we hope with them, some meaningful impact is within Packs, Bags and Luggage, where we are launching an additional luggage collection in the second half of the year. We are just launching also, ahead of the back-to-campus season and the next winter season, a number of new backpacks and models. Our hope is that those will be significant for the future as well, second half launches.

Peter Reilly: That is great, thank you very much.

Magnus Welander: Thank you.

Gustav Sandström (SEB): Good morning, guys. Most of my questions have been answered, but I have one question that I would like to ask regarding the Thule Sleek. Could you give us some indication, as you have had it in the market for some time, on the run rate or development for that stroller, and if you could put in reference to perhaps your Chariot or Glide categories in terms of units sold or trajectory? Thanks.

Magnus Welander: Thank you, Gustav. As we never talk about units sold about anything, I will not do that, but I can give you an indication. We are seeing, in a number of the Central European countries, Benelux especially, the type of sell-through and the type of effects we wanted. We have seen a slightly slower start than we wanted in North America, partly because we came a lot later, so it is going to be very telling now, Q2 and Q3, how the US does. If you look at Northern Europe, the Nordics, we are more or less in line with what we thought, so I would say it is better in some Central European countries, it is worse in the US and it is more or less in line in the Nordics, with what we expected. If you look at that, it is, as I said, very different type of stroller, so it is not comparable in that sense to other things, but it is roughly a little bit behind plan due to the US, but otherwise it is doing really well in the countries where it was launched first, so Benelux and Germany.

Gustav Sandström: Okay, great. Just listening to what you were saying of the army of one, is it fair to assume that the Sleek will have a companion or two before the year-end in the broader stroller category?

Magnus Welander: Not in stores, but that is not a secret. We have told the market we will be showing a brand-new stroller model at the fairs this autumn that will be in store as of 2020, which are also clearly mainstream strollers in that sense, not an additional jogging stroller. It is going to be typical, core, volume-driving mainstream stroller but with, of course, Thule's touch to make it better than most.

Gustav Sandström: Excellent. All right. Thank you so much for taking my questions.

Magnus Welander: Thank you.

I want to thank everybody for taking the time and listening in. I am looking forward to catching up again after the Q2 in July, so I hope you have a very active spring, travel a lot, do a lot and buy a lot of Thule products. Talk to you soon.

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