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Neopost SA (NEO.FR)

Q3 2017 Sales and Revenue Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day, and welcome to the Neopost Q3 2017 Sales Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Denis Thiery. Please go ahead.

Denis Thiery

Chairman & Chief Executive Officer, Neopost SA

Good evening and good afternoon, ladies and gentlemen. Thank you for joining us today for Neopost Q3 2017 sales conference call and webcast. I am Denis Thiery, Chairman and CEO of the Neopost. Jean-François Labadie, Neopost's Chief Financial & Legal Officer; and Gaële Le Men, our Investor Relation Office, have joined me for this call.

We will comment first our Q3 sales performance and then open the call to a Q&A session. The third quarter was below our expectations because the Enterprise Digital Solutions division delivered a temporary weak performance while Neopost Shipping's double-digit growth and SME Solutions' resilience were in line with our expectations.

Now, let's cover in more details each division. Enterprise Digital Solutions' organic growth was only 0.3% due to a disappointing commercial performance by icon Systemhaus and lower new license sales from GMC Software. We are changing the commercial focus on icon Systemhaus and accelerating its integration into Quadient.

As far our GMC Software is concern, the weakness of Q3 is explained by too many changes to the sales force organization at the beginning of the year, following the opening of new verticals. At this stage, the pipeline of license deals is very healthy and we are confident that Enterprise Digital Solutions will deliver sound growth as soon as Q4.

Neopost Shipping delivered again a robust double-digit growth this quarter, a performance that was mainly fueled by Packcity in Japan and the CVP-500. SME Solutions' sales performance is in line with expectations for the third

quarter. Mail Solutions showed good resilience compared to the market, and the SME Shipping and digital activities delivered high double-digit revenue growth.

At group level, we reaffirm that our transformation drivers are in place and we confirm our mid-term objectives.

I will now hand over to Jean-François, our Chief Financial and Legal Officer, who will provide you with more details about the third quarter performance.

Jean-François Labadie

Chief Financial & Legal Officer, Neopost SA

Thank you, Denis. Good evening and good afternoon, ladies and gentlemen. Neopost reported sales of €263 million for the third quarter, down minus 6.1% year-on-year or minus 2.9% excluding currency impact.

The group's organic sales performance came in at minus 2.5% year-on-year. By division, Enterprise Digital Solutions' revenues were stable organically at 0.3% to €33 million in Q3 2017. This situation was mainly due to icon Systemhaus and GMC Software.

On the one hand, icon Systemhaus suffered from the absence of new licenses sales. You may remember that part of icon's business plan was based on our ability to migrate IBM mainframe customers.

In reality, IBM hasn't stopped maintaining its access with [ph] GCS (04:23) Output Management Software contrary to what the company had announced. As a consequence, we are accelerating the integration of icon Systemhaus into Quadient, and concentrating our efforts on Germany, Austria and Switzerland and the limited number of IBM mainframe migrations.

On the other hand, GMC Software recorded slow growth. The reorganization put in place earlier this year to target new vertical markets continued to wait on new license sales in Q3. However, the new organizations are still settled. The license pipeline's quality and volumes are promising. And this provides us with the visibility needed to achieve sound growth in the last quarter of 2017.

Nevertheless, whatever the quality of the growth generated in Q4, the initial target of double-digit growth should not be reached for full-year 2017.

The Neopost Shipping division reported organic sales growth of 11% to €14 million. The division's double-digit growth was driven by the strong deployment of Packcity in Japan and the sale of two CVP-500s. We are seeing that Japan is a particularly dynamic market for Neopost. We delivered the first CVP-500 machine to Yamato. And we are currently deploying automated parcel lockers at the base of 300 sites [indiscernible] (06:05). We are therefore well on track to deploying at 3,000 sites by spring 2018.

Our SME Solutions division delivered sales of €221 million, down 3.3% on an organic basis. Mail Solutions was down 5% on an organic basis, in line with the minus 4% to minus 6% range that we are anticipating. We continue to gain market share in the U.S. and outperformed the market.

At the same time, our Communication & Shipping Solutions activity including graphic were up 7.5% in the third quarter driven by new activities which delivered a very strong performance in the third quarter to reach 19% growth year-to-date, excluding currency effects.

Going into Q4, we are not expecting changes in the Mail market trends and I should also remind everyone about our high comparison basis versus last year.

Considering the recent evolution of the U.S. dollar and the British pound and anticipating your questions, I can tell you that based on current exchange rates, the annual currency impact on sales would be around €25 million with a very limited impact on margins as we are naturally hedged.

I will now briefly comment on our financial situation, which remains healthy at the end of the third quarter of 2017. First, we are well on track to overachieve on our cost savings program of €50 million in SME Solutions by 2018. Second, our cash flow generation continues to be strong allowing us to finance our transformation and to maintain high returns to our shareholders.

Finally on the 24th of November 2017, the Board of Directors have set the interim dividend for 2017 at €0.80 per share in accordance with our €1.7 per share policy. Thank you very much.

I will now hand back to Denis, who will conclude the opening remarks before opening up to the floor for questions.

Denis Thiery

Chairman & Chief Executive Officer, Neopost SA

Thank you, Jean-François. I would like to conclude by confirming that also the third quarter performance was not satisfactory due to EDS. It does not change our midterm ambitions of double-digit growth for our new businesses nor our objective to return to growth at group level. We are now happy to answer any questions you may have.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] We will take our first question from David Cerdan from Kepler. Please go ahead.

David Cerdan

Analyst, Kepler Cheuvreux SA

Yeah. Good evening, gentlemen. I have a few question for you. The first one will be on the Mail Solutions. So the basis of comparison should be stronger in Q4. Do you expect the trend in Q3 to further decline in Q4? This is my first question. And second here regarding EDS, so you expect to rebound of this activity at – do you think that in Q4 you will be able to reach something like 10% or more on a like-for-like basis?

Denis Thiery

Chairman & Chief Executive Officer, Neopost SA

Okay. As far as Mail Solutions is concerned, we do believe that in Q4, again, we will be somewhere in the range between minus 4% and minus 6% as expected. As far as EDS is concerned, we are expecting EDS to come back to a sound healthy growth in Q4, meaning that it will be drastically better than what we have seen in Q3, probably in the range of where we were standing at the end of Q2. And, yes, we expect to get back close to 10% as quickly as possible.

David Cerdan

Analyst, Kepler Cheuvreux SA

And just maybe on Mail Solutions and EDS. For Mail Solutions, can you give us a trend by region in Europe to U.S. and the rest of the world? And for EDS, is there any change in the competitive landscape that could explain the poor performance of GMC for example?

Denis Thiery

Chairman & Chief Executive Officer, Neopost SA

A

Okay. As far as Mail Solutions is concerned, I mean, we have more or less the same situation as in the last few quarters. We see a rather resilient market in the U.S. and this is where we are doing better, much better than in Europe, and this is where we are still gaining market shares and doing much better than the rest of the industry. In Europe, all countries in Europe with the exception of Germany are in the range of minus 5% to minus 8% in mail volumes. And, yes, it has an impact on what we can do in Europe, so same situation. From a market point of view, the U.S. stays strong. From a market point of view, Europe is a problem and, globally, Neopost is doing better than the market, thanks to a very strong performance in North America.

EDS has anything changed from a competitive point of view. No, not at all. All the problems we have had in Q3 are due to the changes that Neopost has done to its sales force beginning of the year. Yes, we did not expect to see such an impact on the ability of our sales guys to close early in the year big deals, but clearly it has been the case. And fortunately, the new organization is efficient. We are starting Q4 with a strong backlog, – excuse me, a strong pipe of deals, stronger than last year at the same time and, yes, we are confident that as soon as Q4 we will see a stronger growth from EDS and GMC especially.

There is one thing that we can say about evolution of GMC and the industry. This is the fact that we are chasing bigger deals than a year ago. The average value of a deal at GMC is higher to date. We are getting close to averaging alpha median piece. And, yes, those deals being bigger, it's taking a bit more time to close them, document them and be in a position to recognize the revenues.

But, no, GMC is still positioned as clearly the leader on this business. We are not losing more deals than in the past compared to the competition. And, yes, again, thanks to a strong pipe of new deals, Q4 will be much stronger.

David Cerdan

Analyst, Kepler Cheuvreux SA

Q

Okay. Thank you.

Operator: [Operator Instructions] Our next question comes from Patrick Jousseume of Société Générale. Please go ahead.

Patrick Jousseume

Analyst, Société Générale

Q

Yes. Good evening, everybody. I have two questions, if I may. The first one is on Temando. I just wanted to have some information about the most recent trends for Temando. And the second question, it's a bit of housekeeping, but when I look at the Communication & Shipping Solutions activities within SME Solutions, you say they are up 7.5% excluding forex when, if I am not wrong, the revenue of this quarter is more or less in line with the revenue of the same quarter last year. So, could you elaborate a bit on that, please?

Denis Thiery

Chairman & Chief Executive Officer, Neopost SA

A

Okay. As far as Temando is concerned, you know that our key priority today is to be able to deploy as quickly as possible with Magento. You know that we have that partnership with Magento. Magento has today something like 250,000 e-retailers using their platform. And the objective is to make Temando technology available on that platform to those 250,000 customers. The plan is to be able to launch officially, I think it's in April of next year. It will be a big event for Magento since in fact they will be introducing what they call Magento 2, which is a new version of their platform, with a handful of key partners including Neopost, who will make their technology available directly under the Temando – excuse me, Magento brand name through the Magento platform. At that point, we are online with expectations, meaning that we are going through a series of review test, tryouts with Magento to be able to launch by April. And so far so good, everything is under control and we should be in a position to launch by end of Q1, beginning of Q2 of 2018.

On the shipping side, I'm not sure I understand your question, the organic growth of shipping including the CVP-500 was in the range of 11% at the end of Q2, is again 11% in Q3 and is still 11% at the end of Q3. And...

Patrick Jousseume

Analyst, Société Générale

Q

My question, Denis, was on – sorry to interrupt you, my question was on Communication & Shipping Solutions within SME Solutions. What I hear 7.5%...

Denis Thiery

Chairman & Chief Executive Officer, Neopost SA

A

Sorry, I understand. Yes, you know that within that category of CSS at – I mean within SME, we have three components in fact, we have the graphics...

Patrick Jousseume

Analyst, Société Générale

Q

Yes.

Denis Thiery

Chairman & Chief Executive Officer, Neopost SA

A

...we have the digital communications side, and we have the shipping side. Shipping and Graphics are technology, which are coming from Neopost, which are controlled by Neopost, either through partnerships or coming from Neopost Shipping and Quadient.

Gaële Le Men-Chagnaud

Financial & External Communications Director, Neopost SA

A

[indiscernible] (19:42) Graphics and Shipping.

Denis Thiery

Chairman & Chief Executive Officer, Neopost SA

A

No, Shipping...

Gaële Le Men-Chagnaud

Financial & External Communications Director, Neopost SA

A

Shipping and Digital.

Denis Thiery

Chairman & Chief Executive Officer, Neopost SA

A

Shipping and Digital Communications, sorry. Thank you. Thank you, Gaële. Those two are the ones that have a big impact on the long-term future of Neopost and within SME. And those two components, again, Shipping and Digital Communications have been growing at...

Gaële Le Men-Chagnaud

Financial & External Communications Director, Neopost SA

A

29%.

Denis Thiery

Chairman & Chief Executive Officer, Neopost SA

A

...29% in Q3 and close to 19%...

Jean-François Labadie

Chief Financial & Legal Officer, Neopost SA

A

Year-to-date. So this is what we were pointing out. Meaning that on the graphics side, we are this quarter again, and since the beginning of the year slight negative.

Denis Thiery

Chairman & Chief Executive Officer, Neopost SA

A

...year-to-date. So, this is what we were pointing out. Meaning that on the Graphics side, we are, this quarter again, and since the beginning of the year slightly negative.

Jean-François Labadie

Chief Financial & Legal Officer, Neopost SA

A

Yes.

Patrick Jousseau

Analyst, Société Générale

Q

Thank you.

Operator: [Operator Instructions] We'll now take our next question from Mourad Lahmidi from MainFirst. Please go ahead.

Mourad Lahmidi

Analyst, MainFirst AG (France)

Q

Yes, good evening. So I have some questions on EDS, please. The first one, can you talk about the new organization and what makes you think that under this new organization the business will be easier to progress? Second question on the slow growth at EDS. Does it have any implication in terms of the margin of EDS? You think that you're going to be able to, let's say, maintain the margin despite the late start of those contract at EDS? Thanks.

Denis Thiery

Chairman & Chief Executive Officer, Neopost SA

A

Okay. Number one, why did we change the organization? First, because we had to integrate into the organization a new vertical, especially healthcare. As we did introduce healthcare, we did split the previous verticals that were in fact, grouped together, we used to have last year only one group of sales guys specialized at the same time in banking and insurance. When we did introduce healthcare, the choice was made to split that group into – to have, on one side, banking which is today one of the key drivers of the growth of GMC and to have a [ph] second (22:34) group composed of insurance and healthcare. Those two are going hand to hand. Most of insurance companies are, at some point, involved into healthcare, insurance and so on.

So, as we did that, the group of sales peoples was put under different management. And there was a [ph] ready provision (23:05) of the customers' portfolio. When you do that, you can expect that there will be, especially at the beginning, some negative impact since some of those sales guys have to start the year from level zero. They are inheriting a new portfolio of customer and they have to start working on it.

It has been the case for those people who move to the new division to the new, I will say, vertical group, insurance and healthcare. And this is where we probably under-evaluate the negative impact, plus the fact that we are choosing today bigger customers, bigger deals. The two combined together explains why it took about nine months to get this – the impact of that reorganization behind us.

Honestly, we were expecting to see an improvement as a stronger performance in Q3. It has not been the case. Deals have not been [ph] lost (24:43), and we are starting again Q4 with a very strong portfolio and we are confident that the growth of EDS, the growth of GMC will get much stronger as soon as Q4.

The impact of reduced growth on the margins, I will speak under the control of Jean-François, sure, it's making it a bit more difficult to improve our EBIT margin in that division. We were expecting beginning of the year, honestly, a double-digit growth for the full year. It won't be the case, but I don't think that it will have a material impact on the level of margin we have reached at that point.

Mourad Lahmidi
Analyst, MainFirst AG (France)

Q

Okay. Thank you.

Denis Thiery
Chairman & Chief Executive Officer, Neopost SA

A

You're welcome.

Operator: It appears there are no further questions. So, at this time, I'd like to turn the conference back to our host for any additional or closing remarks.

Denis Thiery
Chairman & Chief Executive Officer, Neopost SA

Okay. To conclude, I will say that, again, we are very confident that the strategy of Neopost is today helping us to get back to organic growth at group level. The lower performance of EDS in Q3 does not change our potential to get back to growth as quickly as possible at group level. This being said, Gaële, can you tell us what the next meetings will be?

Gaële Le Men-Chagnaud

Financial & External Communications Director, Neopost SA

Yes. But before that, Paul, is there no other questions? No? Okay. So, we all thank you for being with us tonight. Please be informed that a transcript of this conference call will be available on our website shortly. And note, that our next financial communication event will be the publication of our fourth quarter and full-year results to be released on Tuesday, 27th of March after market close. The presentation will be held on Wednesday, 28th of March in Paris.

Thank you again for participating in this conference and have a good day to you. Bye-bye.

Denis Thiery

Chairman & Chief Executive Officer, Neopost SA

Bye.

Jean-François Labadie

Chief Financial & Legal Officer, Neopost SA

Bye.

Operator: This concludes today's call. Thank you for your participation, you may now disconnect.

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