Reckitt Q3 Trading Update

Wednesday, 26th October 2022

Introduction

Richard Joyce

Head of Investor Relations, Reckitt

Welcome

Good morning, everyone, and welcome to Reckitt's Q3 Trading Update. Jeff, our CFO is going to take you through a brief overview of our Q3 performance, and then we will move to Q&A. However, before we do that, I will hand over to our new CEO, Nicandro Durante, who will say a few words.

So, Nicandro, over to you.

Opening Remarks

Nicandro Durante

CEO, Reckitt

Introduction

Thank you, Richard. Good morning to everyone who has dialled in. Before we go through our Q3 trading update, I want to take the opportunity to introduce myself and to provide you with a few messages. I have been at the Board of Reckitt in an executive capacity for over eight years. I already know the business very well.

It has been a privilege to work closely with the Board and the Executive Team over this time to shape Reckitt's strategy as we deliver our purpose, which is to protect, heal and nurture in the relentless pursuit of a cleaner, healthier world. It is a strategy that I fully endorse.

Our brands can make an authentic and meaningful impact to the world, whilst delivering an attractive growth and earnings model. I am very happy to now step into the CEO role for a period of time as we seek a longer-term successor.

Since taking up my new role, I have made a conscious effort to focus my time out in the markets with our people, see first hand how they execute, in stores, with our customers. I have visited a number of manufacturing sites and R&D centres and met many of our leaders. It has been a delight to see the energy and passion of our teams from around the world as they make our brands better and stronger every day.

What I would say is our company is in great shape. We have strong momentum. And Reckitt is well positioned to compete and win in the market and to outperform our peers. The continued execution of strategy is therefore my priority to drive sustainable mid single-digit growth with adjusted operating margins in the mid 20s by the mid 2020s.

Our Q3 and year-to-date results are a testament to the strength and resilience of our business and the hard work and commitment of every one of our talented people. My focus will be on furthering the good momentum that the team has already built, in particular, invest and leverage on large innovations, where the scale and returns are the greatest, review where we can unlock barriers to higher growth, drive the continuation of our productivity and efficiency programmes and drive improved execution in our markets.

Despite very challenging market conditions, which we all have to navigate, we have a significant runway for long term organic revenue and earnings growth from our existing portfolio of fantastic market leading brands. And this will be the core focus of our organisation.

I look forward to catching up with many of you in November and discussing our progress with you all at our 2022 full year's results early next year.

Finally, I know that you are very interested in the CEO search. All I can tell you at this point is that a thorough process is ongoing, and we will update you as and when appropriate.

I will now hand over to Jeff to take you through our Q3 numbers in further detail. Jeff, over to you.

Financial Review

Jeff Carr

CFO, Reckitt

Financial overview

Well, thank you, Nicandro, and good morning, everyone. Our Q3 performance further demonstrates that our strategy is delivering broad based growth across our portfolio of market leading brands.

We delivered a strong performance with like-for-like growth of 7.4% in the quarter, and that is 8.2% on a year-to-date basis. We also continue to see good market share momentum with 63% of our core CMUs either growing or holding share on a year-to-date basis.

Now, given the inflationary environment, growth in the quarter was more weighted to price and mix, a combination of both, which was up 12% in the quarter. Actual consumer pricing was in the high single digits in the quarter, with the balance being driven by a positive mix, mainly related to IFCN and trade spend efficiencies, which have been across the Group.

We continue to mitigate unprecedented cost of goods inflation with our best-in-class productivity programme and implementing responsible pricing where appropriate.

Volume was down 4.6% in the quarter, however, excluding the impact of Lysol volumes, overall volumes remained resilient across the business, and were down 1% in the quarter. Overall, Q3 was another quarter of mid single-digit like-for-like net revenue growth for the 70% of our business, which has been less impacted by COVID. And by the way, this is also true when excluding the positive impact of the competitive supply issues in our North American IFCN business.

This is the seventh consecutive quarter of mid single-digit growth demonstrating the underlying resilience and strength of our business. And this has only been made possible by the exceptional contribution from our colleagues across all of our regions in these challenging times.

Let me cover each of the GBUs in a quick way. In Hygiene like-for-like net revenue declined 1.2% in the quarter. Now this reflects a 3.3% growth when excluding a mid teens decline in Lysol. While Lysol was down in the quarter, this was driven by tough comparatives, where we saw a spike in consumption in August and September of last year, due to the outbreak of the COVID Delta variant.

The periodic decline in Lysol is an improvement versus the first two quarters of the year. And I am pleased that we continue to see strong consumption around 50% to 60% above pre-pandemic levels. Driving the increase in consumption, we continue to see increased hygiene habits among our core users, and a strong contribution from our growth into adjacent categories. For example, laundry sanitizers continue to perform very well with penetration levels in the US now reaching over 10%. We expect year-on-year comparatives to continue to improve for Lysol into the fourth quarter.

In the rest of Hygiene, we delivered robust growth. However, we are seeing some softness in more discretionary categories such as air care. I am particularly pleased to see double-digit growth across our Finish franchise. This is a testament to the investment we are making in innovation, including the launch of our Finish Quantum All in One range.

In Health, we delivered another quarter of growth and outperformance. Our OTC brands continued to lead the way, with around 20% growth in the quarter due to strong consumption and market share gains. Dettol like-for-like net revenue remains well above pre-pandemic levels. Although Q3 revenue was slightly down year-on-year, we continue to expect low single-digit growth for the full year at around 40% above pre-pandemic levels.

Our Intimate Wellness portfolio delivered double-digit growth in the quarter, driven by a strong growth in many European markets, resulting from improved execution and distribution gains. China revenues were lower in the quarter due to the ongoing COVID-related lockdowns.

Within Nutrition, we see the trends from the first half of the year continuing. We continue to see a good turnaround in our ASEAN and LatAm businesses, with strong market share performances across both regions. In the US, we delivered revenue growth of over 40% in the quarter. This included obviously the benefit from the temporary competitor supply issues, which added approximately 20% to our total nutrition business growth in Q3, and 18% on a year-to-date business.

Looking ahead to the fourth quarter, as you will likely be aware the competitor supply issues are starting to normalise and we therefore expect the market dynamics in the US infant formula to return to normal by the end of this year.

Stepping back and looking at the current macroeconomic environment, we clearly have challenging times ahead and with continued high inflation, we do expect some impact in more discretionary categories, as I mentioned, such as air care. It's also clear that with higher energy costs, it will be a tough winter for consumers, especially in Europe. However, it's important to remember that we operate in categories, where trust and efficacy are of high importance, consequently elasticities have been relatively low for the majority of our portfolio brands.

Now moving to the full year targets, we remain on track to deliver against expectations for the year. On net revenue, we have raised the lower end of our range and we now expect to deliver between 6% and 8% like-for-like net revenue growth for the full year.

On margins, we reiterate our target of growth in adjusted operating profit margins for the year. As I previously detailed at the half year, second half margins will reflect higher inflation, more normalised margins in our nutrition business and higher levels of investment versus the first half of the year.

So to summarise, our business remains resilient, delivering a further quarter broad based growth and market share momentum. We have now seen seven quarters of mid single-digit growth, and the 70% of our business less impacted by COVID. And that is also true adjusting for the temporary uplift in our US IFCN business.

While market conditions are challenging, particularly in Europe in the near term, however, our performance year-to-date gives us confidence that we'll deliver our 2022 revenue margin targets.

As Nicandro said, we remain fully focused on executing on our strategy. And we remain firmly on track to deliver our medium-term targets of mid-single-digit like-for-like net revenue growth, and the mid 20s margins by the mid 20s.

With that, we are now happy to take any questions you might have. Thank you.

Q&A

Guillaume Delmas (UBS): So two questions for me, please. The first one is on Hygiene. Because excluding Lysol, the division's like-for-like sales growth significantly decelerated sequentially. I think we are nearly at 9% in Q2, and it was 3.3% in the third quarter. So wondering if you could highlight the main reasons behind this slowdown above and beyond Air Wick? And also curious to hear if you have seen some down trading changes in private label market share development, maybe some delisting in Hygiene in Western Europe in particular?

And then my second question for Nicandro. It is on the Group's strategy. Because Nicandro, you mentioned you were focused on continuing to execute on Reckitt's strategic path. So delivering that mid single-digit like for like sales growth in the mid 20s margin by the mid 20s. So should we interpret this as a clear signal that the Board and of course the leadership team are backing the Group's current strategy? So maybe for the next few years, I mean, until we get to the mid 20s, we should not anticipate major changes to the Group's strategy?

Jeff Carr: Why don't you take that question first? And I will come back to the Hygiene.

Nicandro Durante: Let me talk a little bit about the strategy. Listen, this strategy was lined up around two to three years ago with full endorsement from the Board. And I fully endorse the strategy as I said, at the beginning of my speech. I think that we need to focus more and more on delivering this strategy through innovations, through fantastic execution with our talented people. I think that that should be the focus of the company in the years to come.

I see no reason for changing that. I see that we are in a stage in the company that is all about great execution, with our powerful brands, through our pipeline of innovation. And we have a great pipeline of innovation coming to 2023. So I am pretty optimistic that we can deliver our targets mid long-term.

Jeff Carr: Yes. Just coming back to, Guillaume, your question on Hygiene. The data I have is that if you look at ex Lysol, in the quarter we mentioned the Hygiene like-for-like ex Lysol was 3.3%. If I look on a year-to-date basis, it is 5.3%. So there is a little bit of a slowdown there, but it is largely related to the Air Wick and the air care category really. It is not really a market share issue. It so much is a category slowdown.

So it is not quite as dramatic as you pointed out. It is from 3.3% down from a year-to-date number of 5.3%. And that obviously was higher in the first half, slightly higher in the first half. However, I am not particularly worried. We have seen good performances, for example, in Finish, where we mentioned double-digit like-for-like revenue growth in the quarter. So a strong performance on Finish, strong performance in Harpic and also in Vanish the quarter.

So, all in all, the Lysol number – we talk about ex Lysol because the trends in Lysol are still normalising. The Lysol number was significantly improved sequentially from around minus 30% to minus 15%. And we expect that sequential improvement in Lysol to continue in the fourth quarter as we normalise the business.

Nicandro Durante: And can I add something about the down trading, because you raised the point of down trading here. In general, we are not seeing any material down trading by consumers in our categories. We should not forget that consumers in general, want value for money, and effective products. It is not just low-price products. So, we have not seen any material down trading.

Iain Simpson (Barclays): A couple of questions from me, please. I just wondered if we could dive a little bit into Finish. Clearly, you are happy with performance. Just looking at the Nielsen data that it seems to suggest that in Europe in the US, you underperformed the category pretty meaningfully. However, that does not appear to match with your own comments around double-digit growth and how happy you are with brands. I just wondered if there was an explanation there in terms of channel shift within Finish or anything like that, or whether it is just patchy Nielsen data, and we should not pay too much attention?

And then secondly, in terms of CEO recruitment, I understand that you are a little bit limited as to what you can say, but I wondered if you could give us any idea of timeline and when you thought you might have a little bit more for us in terms of CEO, and just wondering how long that process would take?

Jeff Carr: Let me start with Finish. Finish revenue was strong in the quarter, as we said. And that is largely on the back of the innovation that we have been making with the thermoform technology that we have been rolling out. And we have been replacing our hard-pressed tablets with thermoform product. And that is evident in the Quantum All in One range. That is clearly a superior product. It is premiumized in the category. And we are very pleased with the overall performance.

Now, having said that, market share in the US is not where we want it to be. We are down in terms of market share in the US against an incredibly strong brand. However, we have plans in place. It is early in the relaunch of the innovation. We have strong plans in place. And we believe that we will make good progress as we continue to innovate and continue to drive the thermoform technology. We are happy with the performance today. There is more to be done, especially in market share in the US.

If you look at Europe, we had some issues with one or two customers as we put through price increases, and that affected temporary market share issues. Overall, we are very pleased with our market shares in Europe, and also with our total revenue. You are not wrong; the market share is not perfect. We have some room to go, especially in the US. I think that is a key battleground for us.

Richard Joyce: Yes. Iain, I am not sure whether Nielsen picks up Australia, New Zealand, emerging markets, Eastern Europe. So obviously we are looking at the total picture.

Nicandro Durante: Regarding the CEO, the process is underway. We are reviewing internal candidates and benchmarking external candidates. We will provide a full update as when it is appropriate. However, I cannot provide you a specific timeline because the process will take time. I am here in order to give the Board and the company the timing to find the right person to run the company.

I think that the Chairman has mentioned before that the process may take nine to 12 months but we do not have any timing for that. However, we will take the time that is necessary to find the right person to steer the company for the future.

Bruno Monteyne (Bernstein): My first question is on those numbers, you quoted about Lysol and Dettol versus pre-COVID. I think you said about 50% higher for Lysol. 30-40% for Dettol. Can you just clarify? Does it include the benefit of pricing? Or is that really a consumption volume weighted number? On that, I think from quarter one already, you talked about normalisation stabilisation in these Lysol and Dettol related brands. However, if I think pricing out, it is not just Lysol, that is down materially still this quarter, but Dettol and volume, certainly materially down as well. If we were to define normalisation of stabilisation as stable volumes, when do you expect you will be closer to that, if we use that?

The second one I think you just said before, you do not see any signs of down trading. I sort of agree the price services do not look too bad. However, surely there ought to be some places. If I just look at Nielsen Europe, I know it does not include Australia, Richard, but clearly there still seem to be market share losses to private label as private label is gaining. If you were willing to really scratch hard, where do you start seeing potentially some signs of down trading by consumers to private label or other cheaper brands?

Jeff Carr: Bruno, thanks a lot for your questions. First of all, let me take Dettol, because Lysol and Dettol are in slightly different phases of their normalisation. So let me take Dettol off first. We said in September 2021, that we saw Dettol stabilising at around 40% revenue over the pre-pandemic levels. That is a revenue number that we have never really discussed the volume position.

We continue to see those types of levels around 40%. We expect to finish this year around 40% versus 2019. I think considering we gave that guidance in September, that is pretty consistent. What we also said at the time is we expect Dettol to start growing in 2022. We have had a few mixed quarters. We were down in Q1, up in Q2, down in Q3. However, net-net, we still can see Dettol growing in net revenue in terms of the full year 2022. That has always been a net revenue discussion.

Next, we said that Lysol has been consistently performing at around 50% to 60% in the US point of sales increase versus our pre-pandemic levels. We continue to see that performance. Obviously, as we work through the peaks from 2021, we are starting to normalise versus last year, as I mentioned on the call, down 30% for first off, around 15% in Q3 and we expect that progression to be closer to back to flat by Q4, that type of area. We are very pleased with that overall performance.

Within that, there were some areas winning and losing. I mean, Lysol wipes in the US, for example, has been soft in terms of shares. We had a major competitor which had patchy on shelf performance in 2021. It is also a category which is a bit more commoditised with private label.

However, overall, we see strong share gains on the most important parts of the category, like laundry, like LDS, Lysol Disinfectant Spray. Into the new areas of the brand that we are moving it, laundry sanitiser, we are very pleased with the performance. All in all, those have been revenue targets. I am not going to dissect those by volume. However, we do see Lysol and Dettol normalising, and we expect 2023 to be a relatively normal year, where we would not be talking about the peaks and troughs of prior years. We will be back onto a consistent basis, where we can talk about underlying performance.

In terms of down trading, you are right to pick out Europe Hygiene is one area where there have been some market share gains. Generally, that has been more against the commoditised type of categories like laundry detergent and fabric softeners, and in markets like Spain, which have very strong private label markets. We do see a slight shift in European hygiene to a few basis points to private label but equally, we see private label losing share in the US, for example. We have been gaining share versus private label in the US.

Net-net, as Nicandro said, there is no major gap relative to private label. We are holding ground relative to private label.

Bruno Monteyne: Thank you, Jeff. However, if I just may follow up. I understand the guidance was always on a nominal basis. However, if you say Lysol is still declining at mid teens, let me make that minus 15%, you probably have 10% pricing if it is silent. So I would still suggest minus 25% volumes. Similarly, then for Dettol, surely the volume picture matters as much, I understand the top line and surely when you are in double digit volume declines, that may suggest that kind of normalisation of hygiene habits still has a long way to go. Would you not agree with on that?

Jeff Carr: I do not agree that the normalisation has a long way to go. I think when you look at the new initiatives, when you look at the stickiness of the hygiene habits with our core users, I mean only time will tell if we are able to stabilise these two brands. However, we are in an exceptional time in terms of cost of goods inflation and pricing. Clearly, I said at the beginning of this year, that the growth would be more price-driven than volume driven in 2022. However, I think that is a temporary thing.

I do not think volumes are in decline. I think we have a temporary issue where price is going to be a bigger constituent part of the growth than volume. That is a temporary thing, which, we need to demonstrate during the course of the next 12 months that we can see both of those brands growing. I think we will demonstrate that. And I think that is all we can do in terms of answering that question.

Fulvio Cazzol (Berenberg): The first one is on input cost headwinds. You are guiding to high teens for this year. I was just wondering if that was a subtle change to the H1 results when you expected 20% inflation in H2 versus 10% in H1. I.e., just tried to understand if cost inflation will be closer to 25% or so in H2 rather than the 20% you indicated at the H1 result?

My second one is on nutrition. You stated in the release that you expect to exit the year with normalised sales volumes and margins. I was just wondering if you can clarify what you mean by normalised? I guess I am trying to understand, how much of the 18% benefit there you realised on divisional growth from the competitor issue? How much of that you expect to retain by the end of the year and into 2023?

Jeff Carr: First of all, on input costs. I hope there is no misunderstanding, because we have not changed our commentary at all. It should be totally consistent with the half year. And on what we said at the half year and what we are repeating is that for the full year, we see high teens commodity cost inflation.

The number we quoted at the half year was 15% for the first half, which implies closer to 20% for the second half. That is exactly in line with what we are seeing. By the time we entered the second half, we had something like 80% of our costs pretty much fixed through forward buying contracts or hedging. That has not changed at all.

What I also said is I expect the second half of 2022 to be the peak of commodity inflation. I think based on prices we are looking at into 2023, that is true. That is not to say 2023 is going to get easy. Prices are still high, much higher than if you go back to 2021 or 2020. However, the peak of the inflation, I would say, seems to be in the second half of this year.

The other challenge for 2023 as we look forward to it is that CPI inflation, labour inflation has yet to come through the system. We expect that to be more impacted in 2023. However, in regards to the input costs, we try to be consistent, high teens for the year, slightly higher in the second half than it was in the first half.

In terms of how we see Nutrition coming out, maybe Nicandro.

Nicandro Durante: Yes, a few words about that. We expected that we see already on the shelves the competitors brand coming back. We expect to be normalised by the end of the year. The assumption that we have today is that it will be full supply for the competition at the end of the year. When they say next year is going to be a normalised year, it is going to be normal competition.

Regarding your question about retention, well, we will do our best to retain as much as possible consumers to our brands. Our brand is quite nice strong position nowadays. It is number one brand choice by the physicians in United States nowadays, which is a great place to be.

Majority when a mother already has her baby with a certain brand, they stick with the product. We expect to retain. I cannot give you any guidance for next year about the retention rates, but we expect to be stronger than we were before the out-of-stock situation happened in United States.

How strong? Well, we will be as strong as possible. We are going to work very hard to keep our brand with the leading position that we have nowadays. However, I know as well that the competition is going to work very hard on the other side. We have to wait and see but expect to be next year in a much stronger position against we were before the out of stock situation with a competitor happened.

Jeremy Fialko (HSBC): Couple of questions from my side. First of all, can you talk about pricing and kind of like where you are in the process of actually putting the price rises that you need in order to restore the margin structure of the business. Roughly how much more you think you need to put through when you think that process might end based on where costs are at the moment?

Then secondly, can you just talk a little bit more about the growth of your IFCN business ex the US. I think mid single-digit does not seem such a rapid rate of growth, given the fact there is still plenty of pricing around. Perhaps you could talk a bit about some of the dynamics in those sort of non-US markets.

Jeff Carr: Yes. Let me start on pricing, Jeremy. You will have seen on our price mix numbers that our pricing has increased in the third quarter. And we were relatively low in quarter one with some acceleration in quarter two. We have had quite significant pricing come in through post the second and third quarter. Obviously, that will help us get to the position we need to be by the end of the year.

Now because we have implemented that pricing in the course of the year, we will get quite some significant carryover for that price into the start of next year. I am not going to get into what other pricing we are going to do during the course of 2023. However, I would just emphasise the fact that first place we look is internally with our productivity programme to make sure that we can do everything we can do to minimise the price increases to our consumers. That is pretty much the first thing we look at.

We have, I think, a best-in-class productivity programme, which will keep our foot very much to the gas and continue to deliver against, which will allow us to be really responsible in terms of any pricing we might have to take in 2023.

I mean, on IFCN, what I would just say is that our market shares are very, very strong. In fact, in all of our significant geographies, we are gaining market share in Latin America and in ASEAN with one exception that is in the Philippines and we have a strong programme to get the Philippines back on track. Therefore, I think the number we quoted in the press release is well over 90% of our CMUs in Nutrition are gaining or holding share.

I think our share performance is very strong in most markets. Since Reckitt-Mead Johnson, this is the first time we have really seen revenue growth in the Asian markets. And I am very pleased with that. The reason that we have been able to do that is the fact that we exited China and it has given us the opportunity to really focus on building in the markets where we have strong share positions.

In most of those Asian markets, we are in the 20% to 30% market share positions. Similarly, in LatAm. The fact that we have now exited that China market, where we had a weak market position has really allowed us to focus in those areas to build the brand and to see good performance, and I am very pleased with the performance. Mid-single digits may seem disappointing to you, but I am quite pleased with mid single digits.

David Hayes (Société Générale): Two for me. One on input cost inflation for next year and one on US Nutrition. So just on the input cost inflation for next year, I am picking up on a comment that I saw in the headlines, Jeff, that you made I think in a media call this morning that staff costs inflation will be the biggest element of inflation for next year, which I guess if you take staff costs as a base, that could be up as much as 10 percentage points. That would be about £200 million extra inflation. I apply that to cost of goods sold, that would imply that inflation outlook for cost of goods sold is maybe 3.5-4% tops. Is that the way that you are talking about it in some of those absolute numbers, just want to understand that comment, contextualise?

The second question on US infant formula. Congratulations on winning the Texas WIC contract. I think that started on 1st October that you took it over. Just a question on that on whether you saw inventory building in that state as it switches from Abbott to you in September, where that is part of the dynamic of the US business? Whether there are more contracts that are being reviewed that you could flag that maybe you might win and gain from over the next quarter or so?

Jeff Carr: Okay, David, and let me try and be a bit clearer on input cost next year. And do not take what you read in the press too seriously, please. I think what I meant to say, and I will go back and check my exact wording. However, what I meant to say is we have not seen much staff cost inflation come through yet. It will be a challenge for next year. I do not think I meant to imply it would be a bigger absolute cost inflation than commodities.

I think staff costs, we have not really seen the inflation come through the system yet. I was flagging that whilst the commodity costs will be off their peaks, there will be other pressures such as staff costs starting to come through. I was not trying to get into a situation where I was comparing the absolute increase in staff costs to commodity costs. Whilst commodities are coming down, the absolute levels are still elevated compared to 2021.

We are tracking many commodities, including things like ocean freight, and they are coming off their peaks. However, that still is at a higher level than 2021. Just to be clear, I was flagging that staff costs and CPI would still be a driver of inflation next year, but not comparing the absolute numbers amongst the two.

I do not have a lot to say on WIC contracts in terms of the Texas bidding. We are pleased to take that on board. There were no significant inventory impacts in terms of our performance. I do not think that had any impact on the quarterly performance of IFCN in total. In the normal course of business, WIC contracts come up, and we are keen to bid for them, and we will try and be competitive and hopefully win more than we lose.

Celine Pannuti (JP Morgan): My question is on, you said you were firmly on track for your midterm targets of mid single-digit growth and mid teens margin by mid 20s. I wanted to understand when you look at that versus these challenges of the current environment, what sort of visibility you have in 2023? In other words, we know that in 2023, there will be the impact of the nutrition normalisation. If I put this aside, I mean, what is the visibility on 2023 versus the environment that you mentioned on some challenges, for instance, in healthcare, or maybe a bit of a softer demand and the ability to deliver on that?

I presume, and that will be my second question that is related, if I think about the margin performance this year, which you say will be up and was strongly up in H1, how much of a drag of the tough comparison we should think about as we look into 2023?

Jeff Carr: I mean, let me take those and first of all, I would say I am not going to get into specific guidance on 2023. However, the reason I can say that we are firmly on track is that we have a lot of levers that we can pull in order to develop our margins back to the levels. We are confident on the resilience of the business overall. Air care is a category where we see some softness, but generally, as I look across our categories such as OTC, such as Finish, for example, in auto-dish, I see really resilient brands.

When I spoke in September 2021 about the path to the mid 20s margins, what I pointed out at that time was that most of that comes from developing our top line and the leverage that we get on our fixed costs. We invested in fixed costs in 2020 and 2021; and that brought our margins down.

The fact that we are now growing on the top line, we will get that leverage, and that will be part of the way to driving us to those midterm targets. Of course, in addition to that, I am very pleased with the outperformance that we have had on our productivity programme as well. That remains a key part of the programme. I mean, there is still significant efficiency opportunities that I see here at Reckitt to improve performance and drive productivity.

The combination of those, I feel very confident that we are on track for those mid 20s targets. However, of course, no one is denying that we are going to face challenging times. These are incredibly challenging times for all businesses. We just need to continue to perform and outperform our peers, and deliver in line with the external environments. I think we can continue to do that and have good performance over the next several years.

In terms of the 2022 margins, the best way that you can look at it is if you just take – I leave it for you to do the calculation. If you take the average margins of Nutrition from 2021 and look at the margins that we are going to deliver in 2022, take the delta, if that is the best way that you can estimate, the upside that we have enjoyed from the fact that although we have not put pricing through in Nutrition in the US, the fact our margins have grown is purely due to the leverage of the extra volume that we have been selling and the extra performance that we have had, whilst competitors have been off the shelf. That is the best way that you can do that calculation and come up with an estimate of the normalisation. Maybe I will get more specific on that with the year end results and give more guidance to that.

Tom Sykes (Deutsche Bank): Firstly, could you make some comments perhaps on your outlook for the flu season? How that started off for your inventory building, and where your own capacity is to supply the market during cold and flu, please?

Then just to come back on to the volume aspect, given that the volumes by region, when you look at them in Europe and the developing markets have seen a sort of 7-9% swing quarter to quarter and obviously the developing markets number is down by 7% in volume terms, I know you reference in the report, Lysol and Dettol. However, the price mix is the same in developing markets in Q3 versus Q2, but your volumes have had an 8% swing in terms of the year-on-year growth. Are you happy with the price elasticity you are seeing outside North America? And have we seen the lows in terms of the volume growth, or do you think that volumes could actually get worse?

Jeff Carr: Let me start on the flu question. In terms of our own capability, we have been investing in our supply chain significantly over the last 2.5 years. You have seen our OTC numbers were up significantly over the last three quarters. And I expect that we will be able to meet demand.

In terms of what sort of flu season, we expect, we have seen basically strong flu season in Australia. Sometimes we take that as an indicator of what to expect in North America, but consumption of our cold and flu medications remains very strong. I do not see any reason not to believe that there is going to be a fairly strong cold and flu season and we are ready for it. And obviously, that includes selling in over the September-October period for readiness for that, which tends to peak in January-February timeframe.

We have not seen massive changes in inventory. So there has been no significant movements in trade inventories. So if you are looking into our numbers in Q3, pre Q3, post Q3, I do not think the trade inventory numbers have had a big impact on that.

I think coming to the developing markets and volumes, again, I think you just have to not get carried away with one quarter's performance. So are we particularly worried about price elasticity? No. I think generally, when we look at our overall performance and look at the full year performance, our volumes on a year-to-date basis remain really strong and positive for next Lysol, and next in US, IFCN impact.

Obviously, we did have a tougher period in Q3 in, for example, Dettol in Asia. We are addressing that. We have specific plans in place to address that. As we mentioned, Durex in China, we had a tougher period, partly due to continued COVID effects. And so, in the longer term, no, I do not see particularly concerning around price elasticity.

Our brands are generally in premium categories with strong margins. They are highly efficacious brands, which as we see recessions, as we have learned from recessions in the past, majority of our brands remain very resilient and we expect that to continue.

Martin Deboo (Jefferies): Just a quick build on Tom's question about cold and flu. Just some of your commentary, Jeff. Clearly very strong results in Q3 in OTC, ahead 20%. You seem to suggest that market growth and market share related. However, the Nielsen in the US seems to be showing off-takers sort of pretty flat year-on-year. Can I just sort of ask the question again, how much of that 20% performance in Q3 was sell-in versus sell-out? That will be the specific I would want to ask.

Jeff Carr: Based on the numbers, I am looking at very little. I think if I look at our total cold and flu performance, it remains very strong across all the brands. I will go through brand by brands, Strepsils, Mucinex, Nurofen.

If I look right across the brands, we see strong offtake, both in Europe and in the US. I am a little surprised if you do not see point of sales data, which supports that. By the way, our market shares for Mucinex are at very, very high levels, which is usually the case. We gain market share when there is a real cold and flu issues, because we know our brand is more efficacious than the competition.

I do not see any softness in terms of off-take. Right across our cold and flu brands, we are performing well in terms of consumption. I expect that will continue.

Now the comps, of course, OTC we record plus 60% in the first half of the year. The comps will get best because we are up against fairly strong comps in the second half and certainly in the fourth quarter, we had fairly strong comps in terms of OTC. The comps will certainly soften as we as go on because we are going against tougher comparatives.

The first half of the year, as you recall, was practically no cold and flu season. We had a pretty good second half of the year and we had a pretty strong fourth quarter in terms of

OTC. We will be accounting that in the fourth quarter this year. However, inventory builds we measure and we look at very carefully. We have not seen any significant inventory build.

Chris Pitcher (Redburn): A couple of questions, please. Could you give a bit more colour on the contribution to Lysol sales from the Global Business Services division and new markets? Whether that contribution is up on what it was last year?

Secondly, on the US infant nutrition, are you able to give a split of year-to-date what has been rebated and non-rebated? Certainly, my understanding is a lot of the supply disruption has obviously been won on a non-rebated basis, which has obviously helped you on price and margin and whether if those sales are retained next year, they remain on that attractive margin. I am trying to understand what you think the mix of business likely next year will be between the two different subgroups?

Jeff Carr: Yeah, look, we have developed a strong GBS business, Global Business Services – sorry, professional business, which is focused not just on Lysol but on Dettol and other brands. The contribution to growth this year is not positive. That is largely because of the volume that we have put through in the US with the peaks at the beginning of 2021 and during the Delta variants in 2021.

The volumes in 2021, especially in the professional business, were very strong. We have come off that, but we still have a much bigger business than we started in 2019, and we still see growth going forward into 2023. For this year, it is negative, but that is largely because of the fact that the COVID peaks in the early part of 2021. August, September with the Delta variant in the US was so strong, and that drove very strong sales in 2021.

In terms of IFCN, yes, we have gained both in the WIC business, but also in the non-WIC business. Clearly, where our competitor has not been able to supply WIC in their WIC markets, we have filled that gap and being fully rebated for it. Now, we will lose that business quite quickly once the competitors are able to supply into those markets. That will be a significant margin impact, which is one of the key drivers why we have had beneficial margins in 2022, because we have been fully refunded for that WIC business that we have been selling into markets, which are not our WIC markets.

We will lose that. I think our competitors said they will address the WIC markets quickly. That will be one of their priorities. We expect we will lose that more quickly.

Now, you have still got the issue of mothers not necessarily wanting to switch. However, if they do not want to switch in those markets and they are a WIC customer, they will have to go to a fully priced product, which will be difficult for them. There will be some challenges there. However, I will go back to what Nicandro was saying when we measure our market shares, we measured the non-WIC market shares and we expect to continue to be strong. We are in a better place than we started. This, as Nicandro said, we now have the number one doctor recommended brand in the US that is an important KPI for us.

There is going to be a significant battle coming up, where the competitor looks to get back their market shares but we are up for that and we expect to perform well in 2023, albeit we would not be confident in the numbers that we had this year, clearly we will give some of that back on revenue and margin.

Chris Pitcher: I was going to say can you confirm that Nutrition is ongoing part of the strategy? I know there was some conjecture earlier in the year about a potential divestment but that seems to have been put to one side. Looking forward to next year, it is very much part of your planning. I wonder what you can say.

Jeff Carr: Well, I would just say we have three GBUs, three global business units and they are all core to our strategy. Yes. I do not know, Nicandro, if you want to add anything?

Nicandro Durante: I am saying we are running the business and we are going to run the business the most possible way. We do not talk about those things for the future. However, we have three business units, as Jeff rightly said, and you are trying to get the most of it.

Pinar Ergun (Morgan Stanley): I have three quick follow ups to the debate so far. The first one is, can you please share with us what the volume decline would have been, if you also adjusted it to exclude the US IFCN benefit in addition to Lysol? And what are some of the areas driving this volume decline? For example, do you have anything to call out in Nutrition?

The second follow-up is, which categories other than air care would you categorise as discretionary? And what gives you comfort that demand for those products rather than market shares, but demand for the products will stay resilient in the months ahead as the cost of living continues to bite? If I can squeeze a really quick third one, small one on the financing costs, I believe, around 20% to 25% of your financing is in floating rates? How should we think about that as we head into 2023?

Jeff Carr: Okay. Well, I will trying to answer quickly, but the volume we talked about ex Lysol is down 1%. If you took out the benefits of IFCN, it would be probably down around 2% in the quarter. Still positive on a year-to-date basis. I would just say on the idea that some categories are discretionary, and others are not. It is not black and white.

I think we need to sort of bear that in mind. Where we have air care we mentioned. I could also mention VMS as a category, which has softened as a consequence of consumers being a little bit more conscious about how much money they are spending. Our challenge and what we are up for is to make sure we innovate into those categories to get growth. That is what we will be doing. We have a strong innovation pipeline, both for VMS and air care, which would allow us to gain market share and to grow. Ultimately, the key measure is how we perform versus our peers. That means winning in each of our key categories. Market share becomes important in these times. I am pleased to see that the number of CMUs gaining and holding shares grown in the third quarter versus where it was at the half year.

Finally, on financing costs, you are right to say that we have about 20% of our debt, which is floating, and about 80%, which is fixed. I think that is a good strategic position to have and as a treasury policy. However, clearly that means that as interest costs go up, that 20% floating will incur greater charges and 20% of around 8 billion debt is still quite a lot of debt.

Now, that would not affect 2022, because we are still operating within the guidance we gave for interest costs in 2022. However, clearly, it will be a challenge for 2023. I think most of our peers as well will see increased financing costs, which we will have to manage, as part of one of the levers that we manage as we develop earnings per share expectations. Those costs will go up and we need to manage that.

Karel Zoete (Kepler Cheuvreux): I have two quick follow ups. The first one is on the innovation agenda for next year. You already mentioned a couple of times strong agenda. Most of the time your innovations are brought at premium. Is that still going to be the case in 2023? Or you also be willing to look at some more value innovations, particularly for difficult markets as Europe?

And the other thing I spotted was e-commerce growth was just 5% in the quarter. Is there a specific reason behind it? Is that, for example, China lockdowns? Yes, just looked quite light actually.

Nicandro Durante: Well, the first question about innovation. Yes, we are looking at innovation in different price points for next year. There are products, for example, the health care that you are coming at the beginning next year, but the whole concept is to bring in new innovation and premium position. Then you can drive down the innovation that is in the market in different price points. It is going to be a strategy to meet consumer demand and consumer needs in different price points. No doubt about that. That is necessary.

Regarding e-commerce, listen, it is very difficult to be hang up in a specific quarter to look at the position of e-commerce but of course the lockdown in China had an effect because e-commerce is quite important to China and had an effect in our numbers. However, if you look at nine months, the results are extremely solid and I do not see this is slowing down. I think that we will continue this path of very good performance for the year, for next year. We are very optimistic about our e-commerce performance.

Iain Simpson: I wondered if you could talk a little bit about capital structure. I think on my numbers, you are going to finish this year below two turns net debt EBITDA for the first time in six years. I wondered if you could give any indication as to at which point you might consider capital returns to be appropriate.

Then I just wondered if you could talk a little bit about how retailers are responding to price increases and how that is changing? I think some of your competitors have commented that while taking pricing in the first half of this year was pretty easy. It was getting successively harder as the year went on. You have talked about how raw material costs are peaking in the second half of this year. However, input but non-raw material input cost pressures are building. I am just wondering how we should think about the pricing dynamics through the next six, 12 months, I guess.

Jeff Carr: Well, look, Iain, very quickly on the pricing and retailers. It is never easy to take pricing, and we try everything we can to make sure that we look at every other option in terms of driving productivity to avoid taking pricing. We have taken pricing during the course of this year, some of that will roll into next year, because majority of our pricing was taken later in the year.

I am not going to therefore get into discussions about further pricing that may or may not be necessarily any markets. However, what I would say is that it is never easy to have pricing discussions with retailers. We both have the same goal, which is to give our consumers great offers. Therefore, pricing is never an easy decision.

On capital returns, let me just say, I am pleased with the overall cash generation and performance that we have had, which has been driving down our net debt. The fact that we are bringing our net debt down starts giving us more options. However, I think you have to be cautious about the expectations for the end of this year, because with the dollar at the level it is, we have a significant portion of our debt in dollars. Therefore, we have more debt dollar-denominated than we have earnings dollar-denominated, and that will therefore have a negative effect on our debt to EBITDA based versus where it would have been on a constant rate.

That will have an adverse effect on the net debt to EBITDA due to FX. However, overall, we continue to generate cash and get our balance sheet in a better shape. As we get our balance sheet in a better shape, it gives us more options. It is early to talk about capital returns. However, that is obviously we will keep an efficient balance sheet when the time is right. If we do not see good acquisition opportunities, we have an efficient balance sheet but comfortable. Capital returns in the future will become part of the discussion, but it is a bit early for that now.

Jeff Carr: Have a good day. Bye-bye.

[END OF TRANSCRIPT]