Tarkett FY2020 Results
19th February 2021

Friday, 19th February 2021

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Operator

Operator, Tarkett

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Operator Remarks

Ladies and gentlemen, welcome to the Tarkett FY 2020 Results Conference Call. Today's conference is scheduled to begin shortly. Please continue to stand by and thank you for your patience. Ladies and gentlemen, thank you for standing by and welcome to the Tarkett FY 2020 Results Conference Call. At this time, all participants are in a listen only mode. After the speaker presentation, there will be a question-and-answer session. To ask a question during the session, you will need to press star one on your telephone, where participants may submit a question by typing it into the question tab. I must advise you that this conference is being recorded today. And now, I would like to hand the conference over to your speaker today, Mr Fabrice Barthélemy, CEO. Please go ahead.

Financials

Raphaël Bauer

Chief Financial Officer, Tarkett

Q4 2020 Revenues

Thank you, Fabrice. Good morning everyone. I am now turning to the page 19, Q4 revenues. As you have seen, we are only slightly down organically, minus 1.5%. That is mainly thanks to good growth in the CIS. You know that we are largely residential in that region and demand has been sustained. As commented by Fabrice, this is true also globally. Residential has grown in the quarter; it is also the case in EMEA and in North America. Commercial segments are weaker and we have seen a contrasted situation with healthcare, for instance, trending better, but workplace and hospitality being more subdued. The result in EMEA, we still see some slight decrease, organic. In North America, we are posting a -1.1% organic decrease, but let me remind you that it is comparing to a relatively low baseline in 2019 that had been penalised by the difficulties post our ERP implementation, ACP, in the commercial carpet business. Sport is down on the quarter, less so than Q3, but clearly, we see the impact of projects being delayed or sometimes cancelled.

Q4 Adjusted EBITDA Year-Over-Year

So lower volumes had an impact on EBITDA, but the EBITDA over the quarter is solid. The impact of lower volumes is minus €16 million, but we have been able to more than offset that impact by cost reduction – cost reduction are almost €22 million – both coming from short-term cost flex actions and structural cost reductions.

Raw material prices were still favourable in the quarter, but less so than Q3. It is clearly fading away and we will come back to that. Selling prices were up due to the actions that we have taken, particularly in countries where currencies have weakened or devaluated; the case in Brazil, for instance.

Fabrice commented quickly earlier about the cyber insurance indemnification. It is €15 million, here reported in the one-off bucket of the bridge. This is making up for the loss of margin due to the loss of activity in the second quarter, when part of the activity of the group was stopped due to the cyberattack. So on the full-year bridge you will not see that in the one-off column, but it is being reported under the volume and mix effect to offset the loss of margin from Q2.

FY 2020 Revenues

Moving on to full-year revenues. Organic decrease is 9.5% and it is clearly a stronger negative impact from segments that are more into commercial. It is the case in North America, with minus 15% organic decrease. Conversely, in the CIS, Asia-Pacific and Latin America, we are down only 2% and it is owing to a good performance in the CIS, that is actually stable on a full-year basis.

FY Adjusted EBITDA Year-Over-Year

So EBITDA for the year has been maintained almost stable in value compared to 2019, €278 million, and margin has significantly improved. So of course, we were penalised by the lower volumes; it is €114 million negative effect, so that is quite significant. But the success of the year is that we have been able to almost offset that through cost reductions; €106 million of cost reductions coming both from short-term actions to flex cost, but also to the acceleration of all structural action plans, and that is a €46 million positive effect in the year. We are in advance compared to our plan and it is a real success of the year. On a full-year basis, raw materials were a tailwind of €28.5 million, but that is mostly coming from the third quarter, after the sharp drop of the oil price in the second quarter.

Successful at Flexing Costs in 2020

So in a nutshell, we were successful to adapt to the much lower volumes and that is what we are explaining in the following slide, 23. We have adapted our cost structure very rapidly and very early on, actually; at the very beginning of the pandemic at the end of March. As you can see, half of our costs are fully variable, so the other half is fixed in the short term. Fully variable costs are raw materials and freight, the rest being personnel costs and the other overhead costs of the group.

On the right side, you see that the variable costs have been variable in line with activity, but the rest has been really well-flexed; minus 7% for personnel costs owing to measures such as furloughs, partial work, salary reductions, and all the other cost measures that are benefitting the other cost bucket that we have been able to decrease by 13%. So that is how we have been able to significantly increase EBITDA, margin and reach 10.6%.

EMEA FY 2020

We have also included, in the presentation, some highlights on our key segments, starting with EMEA. You can see here that there is a clear improvement sequentially in the second half, and that is being driven by residential and some commercial segments also, such as healthcare and education, where we see better trends. We commented already that workplace remains penalised. Some countries, actually, in H2 have done particularly well in terms of improving, in the case in France and Germany. We are seeing, in EMEA segment, a very solid margin improvement that is mostly owing to the improvement in the second half, and that is due to cost flexing, structural savings and also lower raw materials purchasing costs.

North America FY 2020

In North America you know that we are more exposed to commercial; I think it is 85% of the activity. So although we saw a really good growth in residential, particularly in the last quarter, organically we are still down 9% in the second half and 14% on a full-year basis. We have taken measures in North America, you know that. We have a new management in place since July. We have also a simplified, new organisation by business unit and we have taken measures to make it leaner, to simplify the support function, the AGNA in particular, and that is giving good results and we are seeing the benefit of the cost reductions. We are also seeing the benefit of the residential turnaround, not only the top line but also in the cost structure. So progress are well on track in North America.

CIS, APAC and Latin America FY 2020

I will not come back to the good sales performance in the CIS and driven by Russia in the CIS countries, and in our Residential, our strong position in Residential there. What is really remarkable is that we have improved, very significantly, the margin on a full-year basis, above 18%, in spite of a negative currency effect. The rouble has weakened throughout the year; however, we have kept our selling prices stable and we have improved margins thanks to solid productivity gains, thanks to cost flexing and also increasing localisation of raw materials. That has given good results and allowed to reduce purchasing costs, on top of the pure effect of oil.

So a really solid performance in CIS, Asia-Pacific and Latin America. Latin America, we have also increased, very significantly, prices to offset the currency devaluation and that is a strong success. We have maintained volumes in Brazil while increasing double-digit selling prices.

Sports FY 2020

In Sports, let me remind you that we are coming, end of 2019, from a record year after three years of double-digit growth. Of course, the pandemic has an impact; it is a project business and we have been quite resilient in the first half, but in the second half we have seen the impact of projects being postponed. We are addressing mainly the education market in North America and, of course, the current lack of visibility leads to projects being delayed.

Once we have said that, sales have decreased in artificial turf, but we have seen good level of demand and, actually, growth in running tracks, but also in the landscape business and in indoor. So there are also some good success in that segment and we are actually quite satisfied with the level of margin, in spite of the sharp drop of activity, above 10%; it is a good level of margin and actually it is quite stable compared to 2019, where we had a one-shot positive effect of an IP settlement that improved the margin that year.

FY 2020 EBIT

So that was the view by segment. Let me give you a few comments on the rest of the P&L before moving on to the cash. Our reported EBIT is down at €47 million, in spite of the stable adjusted EBITDA. You recall end of June we have booked a significant non-cash charge, the impairment of assets for €53 million owing to the weaker outlook in some businesses, in particular the hospitality segment, so we have impaired some of the assets from hospitality. It is also that we have incurred €50 million of restructuring charge in 2020, slightly below what we commented last year, but that has allowed to deliver the cost savings in the plan.

FY Net Income

Our net income is negative, minus €19 million, but that is also owing to the net effect of the impairment charge of the first half. Without that impairment charge, the net income would have been positive at €23 million, and actually H2 net income is positive. There is also one line here that may catch the eye, the income tax line, the charge of €32 million. It is above last year. It is actually owing to two significant non-cash bookings. The first one is a tax asset write-off. We have reassessed the potential to use our tax assets, and in some countries, owing to the lower activity and lower visibility, [inaudible] and written off €6 million of tax assets.

There is another effect which is related to the rouble devaluation. In the CIS, where we report as a functional currency with euro, so not the local currency, the IFRS norms has it that we have to measure the impact of currency fluctuation on non-monetary assets, so our fixed assets, the charge of the factories or machines, and we must book the corresponding tax impact of that fluctuation to defer the tax impact of €7 million negative in 2020. It was €4 million positive in 2019, but it is a purely non-cash impact in tax. It is also the last year that we are seeing that because, in 2021, we have switched to local currency as a reporting currency, functional currency, in the CIS countries.

Strong Free Cash-Flow Generation in 2020

Free cash-flow drivers

The other success of the year, on top of the EBITDA margin growth, is free cash. Fabrice has mentioned the very strong level of free cash flow, €164 million. Actually, the operating cash flow behind that is improving and 2019 cash had been boosted by the setup of factoring programmes for €126 million. Let me highlight also that those factoring programmes are stable, actually slightly up at the end of 2020, so we also are satisfied from that level and we have deployed a few additional programmes.

DOI and CAPEX well-controlled

The strong cash flow is really being driven by the good management of inventory; you can see it on the right hand. A significant decrease in inventory in value, but also in date of inventory. As announced, we slightly controlled CAPEX. We are coming from two years of high CAPEX, both in the capacity, but also productivity, automation and safety, and also IT. Our historical average is more between 3% and 3.5% of sales. So, with the level of CAPEX in 2020, we are contributing to a good cash flow generation and still investing properly in automation, in innovation, as we mentioned, and safety.

That leads to low debt of €474 million, or a reported leverage, including IFRS16 lease liability of 1.7 times, that's the lower part of our mid-term objective, so that is a real success and we are ending the year in a solid situation.

Ample liquidity at year end

It is all the more solid as we have a very strong level of liquidity, €1.2 billion. You will recall that, at the beginning of the crisis in April, we have negotiated additional safety facilities, a short-term credit facility in the form of an RCF of €175 million. The good news is that we have not had to draw on that RCF and it is not drawn at all at the year end. We have set up also a PGE, a Prêt garanti par l'Etat of €70 million. We are fairly contemplating reimbursing that in 2021 and not using it anymore, given the liquidity situation.

Let me remind you that we have no major debt repayments until April 2022, so we have a solid financial situation to start this year, 2021.

Let me now hand over back to Fabrice to comment on the outlook and conclude.

Outlook

Fabrice Barthélemy

Chief Executive Officer, Tarkett SA

Thank you. So, we are clearly starting 2021 with a very strong financial position, low leverage, improved EBITDA margin last year. However, it is not a surprise to you that we have limited visibility on the timing of recovery, especially in some commercial segments. As long as the lockdowns remain in place, even they are partial lockdowns, as long as travelling is reduced or, if not, prohibited, segments like workplace and hospitality are very unlikely to rebound very sharply. So that is why we are basing our scenarios on a muted recovery, spread over 2021 and 2022 and we already know that Q1, in those commercial segments, will remain challenging, especially compared to the Q1 of last year, which was nearly normal, or close to normal, until mid-March.

We still expect that residential will continue to grow well and that should help us. What should help us as well is that not only are we in advance on our plan for cost reduction but we also intend to realise an addition €30 million of productivity targeted this year, in 2021. We are well on track to do that.

We have, however, another challenge to cope with. You know that since the end of last year, actually, purchasing costs of many raw materials and freight costs have soared massively, really very, very rapidly. It is difficult to estimate fully the impact but right now we estimate an impact for the full year of 2021 to about €50 million, so it is a significant headwind.

The good thing is that we have, proactively, started to increase our selling prices since the beginning of this year, so we have not lost any time there. We will increase prices to mitigate that impact but we know that, in some cases, it takes a bit of time, just because, on projects, for example, there is a lag between the time we bid and the time we invoice. That lag can be, of course, 6–12 months.

So, new challenges in 2021. That being said, our mid-term objectives are still valid. We expect to grow above GDP and regain share. We started to regain share and to gain share in some segments. The adjusted EBITDA margin objective is still the right objective, we think, for the business but we have also to be realistic. The timing of that could be slightly delayed due to the headwind we just mentioned, on raw material cost and freight cost inflation and also, of course, the pace of recovery, which is another reason of uncertainty. Nevertheless, that 12% remains the right objective for Tarkett in the short-to-mid term.

On financial leverage, of course, the objective is still valid and we are already, at the end of 2020, very well within that objective, which gives us a lot more room to manoeuvre, if you want and we are really well within that objective.

So, with that, you see, I would say, a cautious optimism. We know the environment is not going to be very easy in the short term. However, having said that, we have very strong fundamentals and what we have achieved last year, in a year that was very special for all industries, gives us a lot of trust and confidence in our ability to implement our strategic plan and win in the years to come.

That was what we wanted to share with you this morning. Of course, I am going to hand over back to the operator for questions and answers, if you have some.

Q&A

Charles-Louis Scotti (Kepler Cheuvreux): Good morning everyone. I have a few questions, five questions exactly. The first one is on raw materials headwinds. How much of the €50 million headwinds do you believe you will be able to offset through price increases?

The second one is still on raw materials. Can you help us modelling the phasing of the impact of those headwinds on a quarterly basis?

The third question, on cost savings. Out of the €44 million COVID-19-related savings in 2020, how much do you think will stay in place in 2021?

The fourth question, on cost savings. You are guiding for €30 million additional savings in 2021. Can you confirm that it will add up to the carryover impact of last year's actions. Also, can you help us quantify the carryover impact for 2021?

Finally, can you detail with us where those €30 million addition cost savings will come from? Thank you.

Fabrice Barthélemy: Thank you, Charles-Louis, good morning. First, I will take your first question on raw material headwinds and how much we can offset. So, just to clarify, the €50 million is our estimate to date and it is a gross impact, so it is before any mitigation. Of course, it could evolve. As you know, the situation is a bit fluid. You heard about the cold wave in Texas that has made things a bit difficult in the short term, in the US, on the supply chain.

If you look at the recent history, I am talking about 2018, when raw material prices increased like that, very steeply, we can offset about 50% during the first year. The good thing is that this year we really started very, very early. I mean we saw it coming a bit and we increased prices, starting in January, so we are very much on time.

We see that the whole industry is facing similar challenges, so we see that in some geographies, like in the US, other players have announced price increases ranging from 5–9%, so very significant price increases. In the CIS, we are the leader and we have announced increases, being the first ones but the market is very likely to follow.

In Europe, it will take a bit more time because there is a higher proportion of projects and on projects what we bid today will be invoiced later, during the year.

Raphaël Bauer: You had a question on the phasing, also, Charles-Louis. It is early in the year, so I cannot be too specific but let me remind you of a few things. You know that, between the oil price and our purchasing price, there is a 2–3-month lag and between our purchasing price and when we recognise it in the P&L, there is a two-month lag, which is our inventory.

So, as we speak, in January, we are seeing purchasing prices going up but still, in the P&L, the prices that we recognise are what we purchased two months ago. So we expect Q1 raw material inflation to be still relatively muted and the effect to be most significant in Q2 and in particular in Q3, actually. So it is more toward the second part of the year but you should expect, already, significant inflation in Q2.

You had a series of questions on cost savings, and I understand it is not easy to factor in 2021 after all the measures that we have taken in 2020, in particular the short-term COVID measures. The way we are seeing it, actually, is that we are looking at a net further decrease of our cost base of €30 million in 2021, based on the cost base of 2020, so that already includes, also, the short-term flex actions.

Of course, some of these short-term flex actions, such as furloughs, salary reductions may not be – may not occur again in 2021 but some of them, typically travel, fairs and exhibitions, some of the way we used to work, will not fully come back. So some of the short-term measures will remain also in 2021, in that perspective.

However, the way to see it is really an additional €30 million cost decrease compared to the cost base of 2020. So, in the sequence, this means that the advance in terms of structural cost reduction that we have taken on our plan, almost €20 million advance at the end of 2020, will be maintained and we will overachieve the initial cost reduction target of €120 million over four years.

Charles-Louis Scotti: Okay, thank you very much.

Pierre Bosset (HSBC): Good morning to both of you. I just would like to come back to your ESG positioning and your recycling and CO2 emissions. I would like to understand how do you hang compared to your competition in your sector, especially against Forbo in Europe or against Interface and Mohawk in the US.

You mentioned tender offer and project-related. How important is it in the tender offer? I imagine not but can it justify a slightly higher price when you have a better environmental offering than your peers?

Fabrice Barthélemy: So I will not comment on a competitor-by-competitor basis. Thank you, Pierre, for your question. I can say a few things. We were the first manufacturer to go 100% phthalate free in all our vinyl products globally. That was some years ago, back in 2012, so we are the first one to be fully phthalate free.

The other thing is that we are also, so far, the only one to have a fully circular solution for carpet tiles in Europe, where we take back and fully recycle carpet tiles at the end of their use, in partnership with a supplier. That, we are the first one to make.

Everyone has initiatives in our industry. We believe we are at the forefront of that ESG commitment, especially on the circular economy.

With regard to customers, I have seen, personally, over the last three or four years, a real change in the way our customers approach these topics. It used to be an add on, very nice to have. Now it is more and more part of the specification and part of the dialogue that they want to have with us. That being said, I cannot tell you you can win a project just based on ESG. You also need to have the right performance in terms of acoustic, maintenance, all the technical performance. You have to have the right service and the right price. However, it becomes more and more a mandatory criterion and especially in some segments, like workplace, like hospitality, where the large customers actually want to achieve a nice ranking.

So far it does not allow a very clear price premium. However, I strongly believe that it will come and especially as regulations become more and more stringent, especially for the end-of-use treatment of flooring products.

Pierre Bosset: Okay, thank you. May I ask another question, just to come back to your €30 million cost reduction target?

Fabrice Barthélemy: Yes.

Pierre Bosset: Will it include another plant closure?

Fabrice Barthélemy: At this stage, Pierre, we do not have any new plant closures announced or in the plan. However, as you know, in the manufacturing industry, we can reorganise production based on the evolution in demand and the evolution in the environment. However, at this stage, in the €30 million, we do not have any plant closures included.

Pierre Bosset: Okay and sorry, the very last question, regarding M&A, do you have, in your pipeline, more opportunities than before COVID or can you comment if there are some competitors which are in a more difficult situation? Thank you.

Fabrice Barthélemy: Yeah, it is a good question. In our pipeline, we have some ideas about bolt-on acquisitions. We are certainly more open to those now that we have gone back to a leverage that is well within our objective. As you know, the mergers and acquisitions market is quite dynamic these days, so it is true that there are some opportunities that come to our attention. We will see how that develops.

Pierre Bosset: Okay, thank you.

Jean-François Granjon (Oddo BHF): Good morning everybody. The first question concerns the top line trend for 2021. It was[?] a good level in Q3, with minus 1.5% for the revenue decrease in Q4. Do you expect positive organic growth in 2021? That is the first question.

The second question, do you expect, despite the raw materials impact, improvement for the EBITDA margin in 2021?

My third question, on the CAPEX level. After the low level in 2020, what do you expect for 2021?

My last question concerns the dividend. Why did you decide to cut the dividend, despite the strong level of free cash flow last year?

Fabrice Barthélemy: So, I will answer those questions. Thank you, Jean-François. As we said, the visibility on commercial segments is a bit unclear right now. However, I would say that, yes, normally, given that there should not be a big impact in Q2, as we had in 2020, we should grow our top line in 2021. Again, we reasonably expect to grow in 2021, unless there is a real fast resurgence of the pandemic, or the vaccine does not work, etc. However, in the current scenario we think, overall, for the year, we should be in positive territory.

The improvement in EBITDA will depend on the scenarios. I think we are very confident with our ability to reduce costs. We started, very early, increasing selling prices. What is less clear is the rise in freight cost, whether freight costs will stay where they are today for the rest of the year or whether they will weaken a bit, the same for raw materials. However, obviously our target is to improve our EBITDA margin. We know this year we are facing some specific headwinds.

The CAPEX level in 2021 might be slightly higher than 2020 but not massively higher than 2020. We are back in a situation where we intend to spend 3-3.5% of sales in CAPEX, which is the average historical level over the last ten years, so we do not have any huge pent-up project that we absolutely need to spend. We are well invested and in all categories, both in manufacturing, in IT and in innovation we are reinforcing. So we are reallocating some CAPEX budget according to geographies and specific projects. However, you can easily model a CAPEX spending between 3-3.5% of sales for 2021 and beyond, actually.

As far as the dividend is concerned, you know we have a controlling shareholder who is a family and who is fully onboard, actually, with that dividend policy and with us they want to put the emphasis on organic growth, first and foremost, so really reinvesting the cash in the business. Later on, we will resume our dividend policy but you know our dividend policy is 30-50% of net result to be distributed. Net result was negative last year so we [inaudible] that dividend policy.

Jean-François Granjon: Okay, thank you Fabrice.

Speaker: We have questions on the improvement in profitability in Maxime Le Floch[?] but I believe we have already answered to these questions.

So, let us move to the questions we received from Elsa Vallou[?]. First question; do you see the same FOREX effect in 2021 occurring as in 2020? Second question; is the new LVT collection unique in Europe, or what makes a difference with peers? Third question; despite the dividend policy, were you allowed to pay the dividend if you wanted? I am referring to the government-backed loan that prohibited it, if drawn. Fourth question; how do you see working capital evolving in 2021? Viewing the low inventory, I would say negative but how much?

Fabrice Barthélemy: The answer, on FX?

Raphaël Bauer: On the FX, yes, thank you for your question. So, on the FX, this year, looking only at the P&L impact, we have had two things. We had the translation effect of the US dollar that [inaudible] us. Then we have the effect of the rouble. So, if we take those two currencies, as we speak, they have stabilised. At the moment, in all scenarios, there is still a negative effect from those two currencies but definitely not the same magnitude of impact as what we have seen in 2020.

If we sum up those two impacts, current year and lag effect in 2020, we are close to negative €25 million. It will not be as significant in 2021, provided those two currencies remain stable and other currencies are not moving in the wrong direction.

Let me remind you also that we have been successful in countering currency devaluation in countries like Brazil, like Norway, the UK also had some price increase to fight currency impact. It is, of course, difficult to forecast but at least in the central scenario the effect is much less than in 2022.

Fabrice Barthélemy: Regarding the question on LVT, it is always difficult to say it is absolutely unique because there are many other suppliers of LVT. However, we think it is a real breakthrough compared to the collections that it replaced, especially in terms of simplicity of choice for the customers between designs and formats, the ability to choose by design and then choose separately the format you want to be able not to be constrained by the format. Also, in the use of digital printing to really improve the quality and rendering of designs. Lastly, with the Tektanium surface treatment, we are really best in class in terms of product performance and resistance to use, whether it’s scratches or stains. So we are really very positive with that LVT line which, once again, is manufactured fully in Europe. You know some of our customers import, today, massively from Asia but we believe that also the current trend on sea freight will be an opportunity for European manufacturers like us to take back some share against Asian manufacturers.

Raphaël Bauer: On the dividend, you were right to point that out. I mean currently the PGE, the state-guaranteed loan, when it is drawn, forbids dividend payments. We also intend to reimburse it quickly this year because, as you said, we have €1.2 billion liquidity, so we do not really need that state-guaranteed loan. I think it is the right thing to do, as corporate citizens, to reimburse these loans that are no longer needed, right now.

In terms of working capital, which was your last question, yes, we ended the year with a low level of working capital but nothing exceptional in that. I mean customers paid on time, suppliers were paid on time and the level of inventory has been reduced but it is a level that is sustainable.

So the only thing that would justify a strong rise of working capital would be a strong pick up in demand. However, we intend to keep a tight control on working capital generally.

Fabrice Barthélemy: If there are no further questions, I would like to thank you all for attending this call today. We are quite proud of the results we have achieved last year in a very difficult year. We know that 2021 comes with a new set of challenges but I think Tarkett, as a group and as a corporate team, has really demonstrated its ability to sail through bad weather, as was last year. That gives us a lot of optimism for the short term and mid-term future.

Thank you again. I wish you a great day today.

[END OF TRANSCRIPT]