ConvaTec Group PLC: 2019 Annual Results and Strategic Update

Friday, 28th February 2020

Welcome

Mark Reynolds

Director of Investor Relations, ConvaTec

Good morning everybody and thank you for joining us today for the ConvaTec full-year 2019 results presentation. For those of you who do not know me, I am Mark Reynolds and I look after Investor Relations here at Convatec.

I will hand you over to our Chairman, John McAdam, who will introduce today's presentation.

Introduction

John McAdam

Chairman, Convatec

Thank you Mark. Good morning and welcome to the ConvaTec 2019 full-year results presentation. I am delighted to be here today and to be joined by Karim, our CEO and Frank, our CFO, who will provide strategic and financial updates shortly.

As you will hear in more detail from Frank, our financial performance is slightly ahead of the mid range of guidance provided in February 2019. As expected, we delivered modest organic revenue growth and profits declined year on year largely due to the increased investment in the transformation.

The transformation continues to move at pace and Karim will expand in more detail. It is still early days but we are making strategic progress and today we will share our new company vision, strategy and operating model, underpinned by a set of core values.

Against this context, the board has given consideration to the dividend and is recommending maintaining the full-year dividend at $0.057 cents per share, reflecting the confidence we have in the future of the business.

Now I'll hand over to Frank, who will cover the 2019 financial performance. Frank, over to you.

Financial Review

Frank Schulkes

Chief Financial Officer, ConvaTec Group PLC

Financial results: performance in line with expectations

Thanks John and good morning. Thanks for joining us today. Let me take you through our financial results in more detail. Starting with slide five, our 2019 performance was in line with our expectations. Group revenue for the year was $1.827 billion, declining 0.3% on a reported basis and taking out the impact of FX and M&A, organic revenue growth was 2.3%.

Adjusted gross margin was 59%, 120 basis points lower than last year. Taking out the impact of FX, we were down 80 basis points, which is the result of negative price and mix, partially offset by positive net productivity. I will provide further detail in a minute. Our operating costs as a percentage of sales increased as expected; this is reflecting the investments related to the transformation, as well as the costs associated with the implementation of MDR. Together, this drove the majority of the total 290 basis points increase. As a result, our adjusted EBIT margin was 19.4%, down 400 basis points from last year. Excluding the non-recurring transformation investments, as well as MDR, our EBIT rate was 21.9%, down 150 basis points. In total, in 2019, we spent $64 million of non-recurring investments in transformation. $40 million was operational cost, mainly OPEX; $20 million was CAPEX and $4 million were costs excluded from adjusted EBIT. We continued to deliver strong cash conversion, achieving 98%, versus 81% in 2018, mostly driven by favourable working capital movements.

We are not expecting cash conversion to continue at this rate, given higher levels of transformation investments, associated CAPEX and MDR in the coming year. Finally, debt leverage in the business has continued to come down to 2.5 times from 2.7 times last year.

2019 revenue: modest growth

Moving to slide six, we experienced growth across all business units, as you can see here. Would care revenue growth was subdued, as expected. Ostomy Care growth improved against a weak comparator and Continence & Critical Care grew above 4%, driven by HSG, which continues to grow faster than the US market. Finally, Infusion Care delivered a solid 4% growth in the year. Reported revenue declined 0.3%, with the difference of 260 basis points between reported and organic growth driven by FX headwinds. This was a result of a weaker euro and British pound, versus the dollar.

AWC and OC: further improvement required

Turning to each of the business units, on slide seven, in Advanced Wound Care we grew 0.5% organically in 2019 and we grew modestly in Q4, in line with our expectations. Organic growth in Q4 was 1.8%, negatively impacted by some phasing of revenue related to Q3 dynamics we discussed in October. Underlying growth was close to 3%. Our AQUACEL foam and anti-biofilm silver products drove the revenue growth. We also launched ConvaMax in the growing super absorber segment. As expected, we saw continued challenges in our legacy products, in particular base AQUACEL dressings and skin care, with hydrocolloids posting modest growth in the year.

We achieved solid performances in EMEA, APAC and Latin America, while the US Wound business continued to be in transition, impacted by the move to a new, specialised sales force during the year. Expected productivity periods are 6–9 months, so we will start to see the benefits of this change and investment in 2020. Call rates in Q4 continue to rise quarter on quarter.

Ostomy organic growth was 1.9% in 2019 and 5.2% in the fourth quarter, albeit against a weak prior year, in particular in Q4. The quarter growth rate also benefited from some one-off tailwinds, including tender timings and a provision throwback, only partially offset by some APAC distributor destocking. The underlying growth was close to 2.5–3%. For 2020, it is important to note that the Ostomy growth rate will be impacted by some SKU and market rationalisations.

Overall, new patient starts in the US have been declining but the most recent data shows that NPS was slightly up in Q4, although this is only one data point and therefore not a trend. As we have communicated before, progress will take time, given the nature of the business.

Traction with our more recent convex product launches, such as Esteem + Flex and Natura Accordion, remain positive, while we continue to invest in and grow our me+ direct-to-consumer programme. From a region point of view, we had a solid performance in a number of markets in EMEA, APAC and Latin America, while the US remained a drag.

CCC & IC: performing solidly

Moving to slide eight, in CCC, revenue growth was 4.1% on an organic basis in 2019 and 3.8% in the fourth quarter, driven by good growth in the Home Services Group. HSG continues to outgrow the overall US continent's market, albeit at a lower level of growth than in prior years. We have seen good volume growth, with GentleCath Glide doing well.

Finally, Infusion Care: revenue grew 4.1% in 2019 and as expected, we had a very strong final quarter, with organic growth of 12.4%, given the change in inventory levels at our largest customer in 2018. We saw strong orders from our customers over the year, driven by continued growth in the insulin pump market.

Margin and cost review: continuing to invest

Moving on to gross margin and OPEX on slide nine, starting on the left with gross margin, gross margin was 59% in the year, down 120 basis points from 2018 and if you adjust for FX and non-recurring transformation costs, gross margin was down 50 basis points, year over year. We saw a positive impact from net productivity gains, which helped partially offset the negative impact of price and mix.

The operational excellence workstream delivered about $25 million in gross benefits, driven by procurement savings, scrap reductions and lean manufacturing improvements. This was partially offset by commodity and labour inflation.

Moving to OPEX, on the right: our OPEX grew to 39.6% of revenues, up 290 basis points, largely driven by the non-recurring investments in transformation and MDR. This accounted for 225 basis points, with the rest coming from recurring transformation investments of about $13 million, mainly in sales and marketing and then, of course, labour inflation. This was partially offset by cost savings.

Our non-recurring transformation investments in OPEX in 2019 were $35 million and these are costs like programme and project management, system-related costs, consultants, training, set up, etcetera, etcetera.

Cash and leverage: robust cash generation and continued deleverage

Finally, moving to cash flow and net debt leverage on slide ten, cash conversion reached 98% in 2019, up from 81% in 2018. As mentioned before, 2019 benefited from improved working capital, largely driven by inventory reductions. Based on increased transformation investment levels and MDR in 2020, I am expecting that cash conversion rates for 2020 will come down to below 80%.

As we discussed in October, we are very pleased we have refinanced the company successfully with a new five-year deal.

A last point from me: net debt leverage in the business has continued to come down to 2.5 times from 2.7 times at the end of 2018.

Thank you very much. I am handing over to Karim now.

Strategic Update

Karim Bitar

Chief Executive Officer, ConvaTec Group PLC

Pivoting to sustainable and profitable growth

Good morning, great to be with you all here today and I want to thank John and Frank for a very helpful introduction and a review of the financial performance. However, what I thought I would try to do this morning was to share with you a little bit of perspective. My guess is many of you are asking, or wondering: Karim, what are some of your initial observations? What did you actually find, having now been at ConvaTec for approximately four months?

I am here to tell you that I am encouraged. You might say, 'Well, how are you drawing that conclusion?' Fundamentally, we worked with the ConvaTec executive leadership team during the course of the last four months or so to really try to assess what were the things that were working well at ConvaTec, what were the things that we could improve? We tried to look at the marketplace: what was happening from a customer perspective? What was happening from a competitor perspective? Then, based on all that, we really drew the conclusion that there were some key things, such as execution and driving transformation that we absolutely wanted to go ahead and continue. However, at the same time, we need to kind of broaden our perspective and really try to develop a vision, a strategy, an operating model, a set of core values which would help us pivot to sustainable and profitable growth.

So what I am going to try to do now is to give you a sense of how did we draw those conclusions? What is it that we actually are continuing to do, based on what Rick had started off and what are some of the things that we are adding, or are new, or are changing?

As we try to pivot to sustainable and profitable growth, what I am going to try to do is give you some perspective as to what is the context. What is it that we actually found, as an executive leadership team. The first thing we found is that, actually, the end markets are very attractive and we will talk more about them. They are large and they are growing. We also found though, that the performance of our businesses was mixed, or varied, that when you looked at the intersection of different businesses and different geographies, in some instances we did very, very well and in some instances we did not do so well. So, that begged the question: what is the root cause? Why were we not being able to go ahead and drive performance in a consistent manner across all geographies and across all businesses?

We identified three fundamental variables: organisational complexity, some limited capabilities and a P&L that was imbalanced. I will give you more flavour to what exactly do we mean by those three observations.

To address the issue and move the ball forward, we mapped out a game plan. That game plan basically consists of a clear vision, a strategy that defines what it is that we are going to do and what it is that we are not going to do, an operating model that helps us execute and drive performance and delivery, then a set of core values that supports that. However, let us go ahead and dig in at this point.

We compete in attractive markets

What you see here are basically four key markets that we compete in: Advanced Wound Care, Ostomy Care, Continence Care, Infusion Care. They are all large, right? They are all in the billions. If you add them all up, then we are roughly at $13 billion. All these markets, fundamentally, are growing in mid-single digits, let us call it 4–5%. So, the first conclusion, or observation, we had is: the end markets in which we are competing are fundamentally attractive.

However, our performance has been varied

How have we been performing, as ConvaTec, in these markets? Really our performance is very varied. If you look at Advanced Wound Care, in fact, we have some geographies where we have been growing: Brazil, Germany. If you look at our R&D capabilities in the area of Hydrofibers and you look at the AQUACEL franchise, there is some really good technology; there is some new innovation that has been occurring in the marketplace. However, on the other hand, if you look at our performance in a key market like the US, we, frankly, have underperformed. If you look at the area of Ostomy Care, we have been quite challenged. You look at our R&D efforts, you look at our operational efforts and the product line could use some refreshing. We have had quality issues in operations. On the sales and service side, we have been challenged. We have been losing share of market in the United States. If you then look at the Continence Care business and the Critical Care business, you realise there is a little bit of a dichotomy. Critical Care has not been, really, growing all that much. Continence Care has been doing pretty darn well and doing particularly well in the United States, working with our Home Service Group.

Then you have Infusion Care, where you have some tremendous R&D, some tremendous technology, the supply chain works well and we have good and strong brand equity with our end customers. So, clearly, you can see there is a fair amount of variance across our businesses when you intersect business and geography. Why is that the case? By the way, that spells opportunity, so I think we need to be very alert to the fact that this variance actually says we can do better, we can improve.

We face some internal challenges

So, three things: first of all, organisational complexity. You might say, 'Karim, what did you actually observe? What did you actually see? What did you draw as a conclusion as an executive leadership team?' Well, what we found, first of all, is that we had a log jam. You say, 'Well, what do you mean by that, at a practical level?' Well, in essence, historically, at ConvaTec, the power really resided with the geographies, so think North America, Latin America, Asia-Pacific and Europe. The geographies had the power and then we started building some franchises, some franchise heads and then we had the functions and it became very unclear who is going to make the final decision, who is going to make the final call? So, frankly, that impedes your ability to execute and to drive results.

The second observation was, when you look at our capabilities, along the value chain – R&D, Operations and Sales and Marketing – they were limited; limited in areas such a sales force effectiveness. When you look at our ability in terms of clinical development and process development, very limited. There is a real need to strengthen those capabilities.

Then you look at the P&L and you say, 'Well, where have you been spending your money?' So here we have a benchmark. We look at our P&L in 2018 and we compare it to all of our peers and we try to get a sense of, 'Well, what proportion of our revenues are we spending on R&D? What proportion of our revenues are we spending on G&A and Sales and Marketing?

You will notice, in our case, on the G&A line, we are spending about 11 percentage points; the average is about seven. The bottom line is we are spending way too much in G&A and we need to be more efficient there. B, in R&D we are underspending, at 3 points. To be a successful med tech company, that is innovation-driven, we have to invest significantly more in this area. If you look at Sales and Marketing, we are spending 23 points, versus an average of about 26 points. We really have to invest significantly more in Sales and Marketing to be able to serve our customers to be able to serve our customers, whether they be patients or caregivers.

We need to serve the distinct needs of patients and caregivers

So, how are we going to do this? Well, we kind of analysed internally what was occurring but we also needed to assess the marketplace. When we looked at the marketplace, we very quickly drew a conclusion that the patient groups that we are talking about, they are very distinct, they are very different patient groups. So, if I suffer from colon cancer, I hope that happens to no one but ultimately if I have to use an ostomy bag, then, guess what? That is a very, very different patient to a diabetes patient who is actually using an insulin pump. When you look at the various caregivers across the board, you will realise that, if I am in Ostomy Care, we are dealing typically with a stoma nurse. If it is Advanced Wound Care, it is a wound nurse. If I am dealing with a diabetes patient, it is a diabetologist or endocrinologist. If it is Continence Care, it is probably a home care provider. These are very distinct patient groups, very distinct providers. So the implication is, there is a real opportunity to tailor your approach to those customer groups.

So, let us see, how are we going to approach the whole transformation? How are we going to pivot to sustainable and profitable growth?

As part of our transformation, we are strengthening our organisational architecture

I shared with you, we want to sort of widen the lens. Originally, the transformation office that Rick had put in place, which is terrific, focused very much on operational improvements, focused very much on how do we improve operations, how do we improve Sales and Marketing, how do we improve Business Services? We had not really lifted ourselves up and said, 'How do we, systemically, look at the entire enterprise?' So what we have done now is to say, 'We need clarity in terms of a vision, in terms of a strategy, in terms of an operating model, in terms of core value.' I am going to share with you how is it that we are going to approach this.

Our new vision

First of all, we work with our employees, over 900 of them and we aligned around a common vision: *pioneering trusted medical solutions to improve the lives we touch*. This is really going to guide the entire direction of where ConvaTec is going. You might say, 'Well, what do these ten words really mean?' Pioneering means we are going to be R&D driven, we are going to be innovation driven, across the entire enterprise, first and foremost. The second thing is we are not going to be a device company, we are going to be a solutions company. We are going to integrate the device, or the product, with service, think real people and with digital. We are going to weave those three things together. However, we are going to make sure that these solutions are trusted, that we have validated these solutions, that we run these clinical trials because no patient wants to be a guinea pig, right? They have to be reliable. Why do we do that? Because we want to improve the lives of the people we touch. All of our offerings, literally, physically touch a patient but we touch them more than just physically. We touch them emotionally, socially, psychologically and there is a real opportunity there, as we think through from a design perspective, what is the solution we want to provide?

Five key pillars

The question is: how do you take this vision and make it reality, tangible, meaningful? We have developed a strategic framework that basically says there are five key pillars. The first thing we are going to do is we are going to focus. We are going to focus on key categories, product categories and on key markets. We have identified 12 key markets we are going to focus on and I will talk to you more about that. Four key categories we are going to go ahead and play to win: Advanced Wound Care, Ostomy Care, Continence Care and Infusion Care. In terms of innovation, we have decided that we are going to significantly increase our investment in innovation, in fact we are creating a whole separate function. Literally, last month, we were able to recruit a very talented Head of Innovation and R&D: Divakar Ramakrishnan. I have known Divakar for quite some time. He is an incredibly talented individual. He has a PhD in chemical engineering with a Harvard MBA. This fellow basically ran all of Lilly's device business, was a Chief Digital Officer and prior to that, had run all of process development, across all of Lilly. He is truly unique, in the sense that not only does he understand product development and the device world in digital but also process development: process development meaning you need to understand how to make something that you can make efficiently and reliably, with quality. You cannot only think about the design from a patient perspective. So you need process development and product development; then you are going to have to combine that with clinical. That is the way you come up with a solution. He happens to be very marketplace-oriented and frankly just collaborative by nature. So I am delighted that he is leading that effort and building this new function.

Thirdly, we need to simplify our operations. What we need to do is to make sure that our operations are customer centric, that they are focused on those distinct customer groups, those distinct patient types, those distinct providers. We need to make sure that we are a lot more agile, that we can respond much more quickly to these customer needs. Lastly, we want one single point of accountability. If I am an Ostomy Care patient I want to make sure that there is one individual at ConvaTec that we can hold to account for how that business is doing and that is Mani Gopal, or David Shepherd in the case of Advanced Wound Care, etcetera, etcetera.

Fourthly, we need to build some capabilities. We need to build some capabilities in areas like process development, in areas like clinical development, in areas like quality and sales force effectiveness. We have not invested in building that muscle tissue and we need to be cognisant of that.

Lastly, we need to execute like there is no tomorrow. One of the great things that Rick did was to put in place a transformation office, with a heavy, heavy focus on executing, whereby there is real clarity as to what is the business case, who does what by when, metrics and milestones. Every week, we check that that execution is there. We are going to be relentless and sustain that endeavour because that is going to help the strategy, frankly, come to life.

Focus

So, focus: we are going to invest in 12 key markets. The USA and China are must-win. They are amongst these top 12 markets. There are an additional 40 markets where we are going to compete and we are going to go ahead and invest in. There are about three dozen markets where, fundamentally, we are either going to exit, places like Venezuela, places like Uganda, or, frankly, serve those markets in an indirect manner, via distributors or via agents.

Innovate

Solutions: we are going to need to build out our clinical development capabilities. We need to combine devices with services with digital. Again, I am delighted that literally this week we named our Chief Medical Officer and Chief Innovation Officer: Dr Jacob Agris. Jacob, to give you a sense, is a neurovascular surgeon trained at the NIH and he also happens to have a PhD in electrical engineering, okay? So, he and Divakar will be working very, very closely as they go ahead and really up the ante on the innovation front and really, truly deliver on this concept of solutions.

Simplify

So, how is it that we are going to simplify our operations. Well, as we thought about, I told you that we are striving to be a lot more customer-centric, a lot more agile, a lot more accountability and a heavy focus on innovation. So, here is the structural side of the new operating model. First of all, we have six global business units. Four of them, you will notice, are the product categories. There is one single point of accountability. That individual, for example Kjersti, is responsible from patient all the way back to R&D. She makes the call across the entire value chain: whatever needs to happen.

Global emerging markets: we have merged together Asia-Pacific with Latin America with Africa and Middle East. Those markets are very similar in terms of the challenges they have.

Home Service Group is a segment which is very, very important and so therefore we want to elevate the importance of how the Home Service Group collaborates with those four product categories because there is a real benefit to doing that as we think about solution. So, this is really a key service arm as we drive the whole solution concept.

Two, notice that Innovation and Technology, a totally separate function, single leadership under Divakar Ramakrishnan.

Then, lastly, quality: what have we done? We are integrating quality with the operations and with regulatory, to build in quality up front.

Then, finally, you have your customer-supporting functions.

Hopefully, you are getting a sense that it is a lot more customer-centric, this model; it is more agile, there is more accountability and we are elevating the importance of innovation, consistent with our strategic framework.

Build

We need to go ahead and build some core capabilities across the value chain: process development, clinical development and R&D, for sure. In areas such as supply chain, we need to work on quality. In areas such as marketing, we need to make sure that we are leveraging the whole digital platform arena. In an area like sales, we need to have sales force effectiveness, be very, very consistent: single platforms for CRM applications, a single platform for improving our service capability, etcetera, etcetera.

Execute

Lastly, for FISBE, focus, innovate, simplify and build, you have to execute. We have to execute all of these initiatives, so we have a transformation office, we have over 100 initiatives underway. As an example, we are in the midst right now of increasing our footprint in US Advanced Wound Care. We have dedicated sales forces now. We used to have just one single one, now we are dedicating it across three key segments: the acute segment, the chronic care segment, the long-term or home care segment, right?

CRM: we literally, during the course of this year, or 2019 I should say, have been implementing one standardised customer relationship management system across Europe. Now we will rolling that out on a global basis.

We need to drive new product introductions and I could keep on going on with more and more examples. However, just know that this 100-plus initiatives, we literally have who, what, when, what metrics and milestones and we track it on a weekly basis so that we can ensure that we increase our say/do ratio. It is very, very clear to me and the executive leadership team that ultimately what we need to do is deliver and deliver and deliver.

Our new values will underpin our vision, strategy and operating model

Okay. So, what are the core values that are going to underpin the vision, the strategy, the operating model? We have identified five core values. First and foremost, if you start about 12 o'clock or 1 o'clock, however you want to look at your clock, it is improve care. We are going to be obsessive about improving patient care. That is at the centre of everything we do. We need to focus on what are the unique patient needs? How can we develop solutions for them in collaboration with caregivers?

The second thing is we need to deliver results. We need to deliver results for our patients; we need to deliver results for our shareholders.

Thirdly, we need to grow together. We need to develop and grow our employees, invest in our employees, work on teamwork so that we can go ahead and serve.

Fourthly, we want to create a real sense of taking the initiative, owning it, do not wait and then lastly, we want to make sure we do the right thing: we do the right thing by patients, we do the right thing by colleagues, we do the right thing by our communities, we do the right thing by shareholders.

To realise our strategic intent of pivoting to sustainable and profitable growth, we are investing

Now, if you sum all this up, you say, 'Okay, Karim, I have understood pioneering trusted medical solutions to improve the lives we touch. I understand FISBE: you are going to focus, you are going to innovate, you are going to simplify, you are going to build capabilities and you are going to execute like there is no tomorrow.'

Well, we have to sit down, as a team and assess, from an investment perspective, what is going to be required to get the job done? What we were able to conclude was that there were some significant opportunities, that some of the investments that we had planned on making were really good. So, for example, GBS, Global Business Services, where we can drive efficiency in human resources and in finance, we absolutely are going to continue doing that. So you see that in the original $150 million. However, we have bumped that up to $210 million and you say, 'Well, why do you need the $60 million more for?' Well, as we reorient the model, to these business units and the innovation function, etcetera, there is going to be some need for some non-recurring investment, not only as we reorient that model but there are opportunities, frankly, that we see, for example, to drive quality and efficiency in operations, where we can invest a lot more in automation. We have really held back on those kinds of activities for a variety of reasons.

The second thing is that there is some recurring spend where we see significant opportunity also, so there we are saying we want to invest $75 million, as opposed to roughly $50 million. We see some real opportunities. We see some opportunities in R&D, frankly, to refresh the entire portfolio. So we need to invest in process development, in the clinical trials to be able to get regulatory approval, to be able to get reimbursement and access.

On the sales and marketing side, there is a real opportunity to go ahead and invest in markets like China. It is a huge opportunity: strengthen our position in the United States, invest in applications and IT systems that can improve our service. If you want to improve service, believe me, the engine of service is having IT and application platforms that support that and that is exactly what we are going to be doing.

Then you say, 'Well, great, we are going to invest all the money, Karim; what benefit are we going to derive from it?' What you see me telling you is that we have bumped up the benefit from $130–150 million all the way up to $150–170 million. This is in 2021 and so it is important to note that these investments are going to bear even more fruit beyond 2021.

In summary: starting to transform ConvaTec

So, at this point, let me try to summarise where we are at. Hopefully you will have gotten a sense of, in the discussion with Frank and I today, is that in terms of financial performance, we are on track. Revenues grew 2.3%; profits were down, as expected.

In terms of the transformation, hopefully you are getting a sense that it is very much at pace. This new operating model, we have already started implementing it; we have rolled it out in February; it is up and running, to give you a sense. So this is not just a bunch of talk about things that we will do. The hundred initiatives? They are actively occurring, right at this point. So what is going to be happening with the transformation, which is all focused on how do I go ahead and pivot to sustainable and profitable growth? That pace of execution and drive is just going to continue at a relentless pace.

Then you might say, 'Well, Karim, what should we be expecting in terms of financial outcomes in 2020?' Well, we are expecting to go ahead and grow revenues. We are going to grow our revenues between 2–3.5% in constant currency in 2020 and our EBIT margin in constant currency is going to be somewhere between 16–18%.

On that note, I am going to say thank you to everybody.

Q&A

Sebastian Walker (UBS): Hi there.

Karim Bitar: Hi Sebastian.

Sebastian Walker: A couple of questions from me, please. Just in terms of the growth acceleration you are guiding for in 2020, could you comment on what are the key drivers of that? Then maybe could you comment on some potential headwinds that we should be thinking about in 2020?

Frank Schulkes: We probably need to click through the different global business units to get the right perspective. So, starting with Wound, as you heard I think it is absolutely critical that we are going to start to see the returns and benefits of the change of our model in the US. We moved to a more specialised sales force and that investment should start to give returns in 2020. So that is a very important element of growth for the Wound business.

At the same time, as you know, we are going to face the full-year effect of the French reimbursement cuts and we are also facing, in Germany, the fact that silver will very likely not be reimbursed any more, starting sort of mid-year but that will probably have an impact for the full year. So, on the positive side, we expect to start to see returns on the US Wound business but there are some headwinds that you can see.

In Ostomy Care, we did about 1.9% for the year in 2019. As we have discussed several times, Ostomy Care, the character of that business is that the trajectory up or down is relatively slow; you do not change the trajectory overnight. So we expect very slow, over the next several years, improvement there. At the same time, we are going to see a negative impact in 2020 because, as part of simplification and focus, we are going to cut SKUs and we are going to go out of certain markets. Overall, that will have an impact to, probably, north of 100 basis points for that business. In CCC, I expect a pretty normal year. You can expect growth rates that we have seen in the past. Also there, though, there will be the impact of market and SKU rationalisations. Then, finally, in IC, we have, of course, seen, in 2018, quite some dynamic related to our biggest customer, the Animas exit in 2019, so we expect that 2020 will be a more normalised year; we should see okay-to-good growth rates in that business, in line with the growth that we see in the overall pump market. Is that answering your question?

Sebastian Walker: Yes, that is helpful; thank you.

Frank Schulkes: Thank you.

Sebastian Walker: Then, Karim, maybe just thinking about the recurring OPEX spend and the additional recurring OPEX spend in 2020, could you maybe comment? We saw Wound investments last year; is there anything tangible you can point to for 2020 and what kind of time period should we expect a return on those investments? I will also try and squeeze one in, which is just: you have not talked about any M&A and there have been some discussions about a Critical Care disposal. What are your thoughts on that?

Karim Bitar: Look, I think, on the investment in R&D and in sales and marketing, there are series of investments that are sort of already in flight, right? So, for example, on the Advanced Wound Care side, we are in the midst of rolling out AAA for surgical cover dressings. This is a sort of very new and advanced hydrofibre. It has the silver in there but it also has the whole anti-biofilm aspect to it too, so we are very, very excited about this. It is one of the new product launches and clearly the transformation has been investing there.

So I think there are going to be more of those kinds of opportunities. Frankly, we need to let Divakar get situated and what I anticipate is that, during the second half of 2020, we will be able to be a lot more explicit as to, 'Well, what is your R&D strategy? Where exactly are you going to spend it and how are you going to spend it?' So really what we tried to do in the first several months was to really develop a strategic framework to guide us. However, my expectation, frankly, is that each and every business unit will be able to, in detail, outline, 'Well, what are we doing to focus? What are we doing to innovate? What are we doing to simplify? What are we doing to build capabilities? What are we doing to execute?'

So I think what is fair to say is that there are more opportunities, frankly, than funds available, which is a good thing. So what Frank and I will be needing to think through is how do we, frankly, prioritise those investments?

On the M&A question what I would say is the following: it is that fundamentally, we want to drive an organic growth strategy? I mean that is what we want to be about, right? So, really, on the inorganic side, we really see the inorganic side as there is an opportunity to try to win in certain key franchises or businesses, if they are some bolt-on opportunities, whether they be technology-driven, capability-driven or geographic, we will seriously consider those. However, those will be sort of in addition, if that makes sense.

I hope I answered your question.

Sebastian Walker: And divestitures?

Karim Bitar: Yes, sorry, on divestitures, as we look in the entire portfolio, we are doing this within the product categories: are there opportunities to rationalise the portfolio? I think it is just good business practice to drive efficiency and take out complexity. Then, within product categories, we are always assessing and analysing. So what I would just say is that is something that we are doing and will continue to do proactively.

James Mainwaring (Stifel): Hi, I would just like to just sort of get a bit more detail on the sort of China strategy. That sort of region has been a sort of area you have been reasonably sort of under-penetrated in. I just sort of want to get a sense of what sort of business model you would be looking to do there. Is that kind of investment in boots on the ground and your own distribution model? Is that sort of partnership or kind of indirect to begin with? What sort of timeframe would that investment be over?

Karim Bitar: Look, I think, with China, it is very clear that it is a large opportunity; I think you do not need to be a rocket scientist to draw that conclusion but there is significant growth that is going to be occurring in China. There is growth in terms of demand but it is also from a technological development perspective, so clearly we want to have our own presence there. We have about, already, a couple of hundred people on the ground but when you look at the proportion of revenues and profits that we generate from global emerging markets relative to our peer group, it is too low. It is absolutely too low. So we have not, frankly, invested in what I will call a direct, primary demand realisation model. We have, historically, been over-reliant on the indirect distribution model. Obviously, that primary demand realisation approach, you cannot do that across all markets. However, when I listed for you 12 key markets we are going to focus on, I can tell you five of them are in emerging markets and so there is a significant opportunity. Now what you are going to need to do is to be very, very astute and think through, 'Okay, well, who am I actually going to target? Am I going to target all 10,000 hospitals in China or maybe there is a subset that I need to really target and I need to really win in. Am I going to do this all on my own, or am I going to maybe collaborate?' We need to assess those options and so I do not want to sort of jump the gun but we have a very, very talented leader in Supratim Bose, who is very seasoned, very experienced in running global emerging markets. He has, frankly, built up a really formidable team now, during the course of the last year, in all of our geographies, so I think that we will be able to provide a lot more clarity in terms of what will be our commercial, go-to market strategies. However, I think it will be a combination of being present on the ground, being highly targeted and also trying to think creatively about the whole alliance piece of it.

Veronika Dubajova (Goldman Sachs): Hi there, the first big picture, if I can, Karim: just thinking beyond 2020, obviously you have outlined a desire to invest more into the ongoing business but I am just curious. I think your predecessor talked about two things: one, 2020 would be the margin trough, so I am curious if you can confirm that is still how you are thinking about it and two, your predecessor talked about accelerating the margin improvement and getting back into the mid-to-high twenties. Is that still a realistic proposition and how are you thinking about the timeframe towards that, if you can maybe help us think through the margin profile beyond 2020 into the medium term?

Karim Bitar: Yeah, so maybe on the first question: is 2020 going to be the trough here, then what are the prospects for margin expansion above and beyond that? Maybe I will let Frank take a stab at it, then I will add to it.

Frank Schulkes: Yeah. So, we indeed have communicated this in 2019 and we believe that 2020 is going to be the bottom. Our focus, I think, is very clear. We are investing now to get the revenue growth engine going, with the associated EBIT dollars, okay? So our focus is: invest to get revenue growth going and then drive EBIT dollar growth in the future. That is starting in 2021, given that 2020 is the bottom. Then, beyond that period, margin expansion will follow. We are not, at this moment, putting a specific timeline on that. I think our first focus is revenue growth and associated EBIT dollar growth for this business.

Karim Bitar: I would just totally reaffirm what Frank said. Bottom line, we need to get to revenue growth at least commensurate with what the market benchmarks are; I think we all know them in this room. Frankly, once you achieve that, thereafter, you can frankly start thinking about margin expansion opportunities. But fundamentally, it is going to be drive the revenue line, so you can see earnings growth and then come back to the whole margin expansion side of it.

Veronika Dubajova: That is very clear. Then my follow-up is on the $75 million of transformation investments you are making. Can you help us understand, proportionally, what is going into R&D and what is going into selling and marketing? Then, as you think about the R&D and SG&A, I think, frankly, ConvaTec has not really brought a meaningful innovation into the market for a while, so I would just be curious, from your seat, to understand when do you think we start to see an improved R&D cadence out of the organisation? When can we start looking forward to some new, differentiated, portfolio and product offerings?

Karim Bitar: I am going to let Frank take the first part of your question; I will try and answer the second.

Frank Schulkes: Yeah, sure. So, I would say, when we look at all the programmes that we are managing, the majority of that $75 million will go into more commercial programmes, sales and marketing, more firepower on the target in the, for instance, key core markets that Karim talked about. Then there is a smaller portion of that going into product development at this stage. I think Karim has been very clear, with Divakar coming in, we will be able to provide more detail, or more direction of travel and a quantification of that later, when Divakar has really laid out his strategy around product development. However, I think the intention is clear: product developments, R&D investments, are going up and we are going to partially fund that through, for instance, the G&A angle.

Karim Bitar: What I would say, Veronika, is we are trying to be very practical, right? The reality is, when you look at the value chain, where you are going to get the fastest response to the marketplace is going to be, frankly, in the marketing, sales and service, right? So, short term, there is going to be a propensity toward doing that. For you to refresh a product portfolio, particularly with the history and context we have, it is hard work, right? There is some heavy lifting to be done, so I do not want to kid anybody and say, 'Yeah, within the next several months, we are going to have refreshed the portfolio;' that is just not real. The reality is that I think that is going to be much more of a medium-term gain, so there will be some low-hanging fruit within the current offerings. I call those, sort of: can we come up with version 1.1, or 1.2, pretty quickly? We have them very clear in our mind, okay? Whether it be in Continence Care, whether it be in Infusion, they are very, very clear in our mind.

So I think those, the 1.1, the 1.2 types of improvements, in the next 24 months, realistically. It will vary depending upon which one I am talking about. If you want to move into what I will call the 2.0, 3.0, you are going to be much more in a 24–48 month timeframe period; that is the reality.

Veronika Dubajova: Sure, thank you.

Paul Cuddon (Numis): Hi there guys. I just have two questions. You have raised the gross benefit target to $150–170 million but could you just flesh out, really, what that means, give us a baseline assumption that you are using to make that calculation and kind of where you see that being generated? Then I have one other after that.

Frank Schulkes: Yeah, so, as I said before, we are tracking all the projects here and the benefits are going to fall in the specific workstreams that we have identified before. So we are going to raise our investments, for instance, in the area of commercial activity, more feet on the street, so that will result in a higher growth rate in terms of revenue and associated dollars. We are also investing more because we see opportunity, for instance, in automation, as Karim mentioned, in the overall operational area, supply chain area, so there will be some more favourability coming out in, specifically, cost of goods sold and some of that in OPEX.

Then, finally, we are also going to expand in GBS; we are going to expand the scope, although the payback of that will be typically a little longer, so we will not see a lot of that in 2021. However, as Karim also mentioned, 2021 is not the end station; it is just a moment in time and we will see the benefits continue to grow beyond 2021 and 2022.

Paul Cuddon: Okay. Then, on the Home Services Group, you have obviously pulled it out as a separate division now. To what extent does the Home Services mandate extend outside of the US? Assuming that it does, there are a lot of homes, just generally, around the world. So how do you do that organically, versus inorganically?

Karim Bitar: It is a great question. The short answer is the mandate does extend beyond the United States and the mandate within the United States is broad. Today it has been heavily focused on Continence Care; what does that mean in practical terms? We are in the midst of developing that. So, again, what I would expect in future sessions is to be able to better articulate for you exactly in terms of where you want to compete, in what categories. what geographies and how are you going to go about doing that? However, clearly, we have a formidable capability there, right? So, coming in new, the levels of service that we can provide our patients are truly world-class. Some of you may be familiar with a metric called Net Promoter Score, which basically measures customer loyalty. When you go visit with the folks at 180 Medical, which is part of the Home Service Group based in Oklahoma City, I spent a couple of days with these folks during my visits, you are really, really impressed as to how they think about service. They have literally broken down the whole service model, just like you would an assembly line. So you will have some systems, some IT systems and you will have some very unique people who will deal with 1,500 payers. They are all very calm, they are all very analytical, they are all very detail-oriented. Then you will shift to the folks that actually deal with the patients. You would want to be best friends with these folks, so you can imagine these folks have been selected in a certain way, so you get Net Promoter Scores that, frankly, are higher than Apple and higher than Disney. The level of customer loyalty is really, really high, so the question is: how can we leverage this capability, right? How can we leverage it across our portfolio and are there opportunities above and beyond the United States? The honest answer today is that is a question mark. However clearly, by elevating it, it gives us the ability to assess what are those opportunities and how can we, frankly, leverage this whole service aspect?

Amy Walker (Peel Hunt): I will try for two as well, if I can, please? Just to pick up on Paul's HSG question, you mentioned, I think, Frank, that it had been outperforming the market growth in the US. However, it sounded as though it is starting to mature now. On what timeline do you think that maturity comes to fruition? Is it about penetration, is there more you can do? How much longer can it outperform the market?

Frank Schulkes: That is very tough to answer. Let me explain why rates have come down and part of that is just simple math. When you grow bigger, 1% growth means, in terms of dollars, a lot more. However, my view of life is I think that HSG will be able to outgrow the market for some time. We are not talking about massive outgrowth but because of the model that Karim just described, the very high customer loyalty, very high penetration in insurance contracts. It will be, indeed, coming down and eventually get close to market but for me it is very hard to pinpoint to a certain date on that. I do not know if you have certain views, Karim, on that.

Karim Bitar: No, I would just say, for me, from a short to medium term, I cannot look at long term right now but I think there is definitely growth there.

What we have basically done is we have focused on one category, Continence Care and one geography, the USA. So, within that intersection, yeah, I can see where the question is coming from but I think there is significant opportunity above and beyond that.

Amy Walker: Okay, thanks. Then the second question is just on execution and accountability, which were key themes in your presentation. Can you tell us what some of the main key performance indicators you both personally, at the C Suite level, are tracking for each franchise, if they are different? How concentrated are those within the businesses? Is it you are tracking a lot of small things that you hope will aggregate over time or is it two or three major things that you are concerning yourself with?

Karim Bitar: There are a handful. We bucket them in terms of voice of the customer, voice of the employee and voice of the business. To give you a flavour for what we might be looking at in terms of voice of the customer: new patient starts. That is a really important metric to us because it gives us a sense of what is going to be happening in the future and it is a really good lead indicator. Net Promoter Score: what kind of customer loyalty might we have? Quality: so we have some very basic, or single-quality, metrics, right? Those are just: let us hear from the customer, how are we doing? Voice of the employee is really simple, I mean: what is the level of engagement? We are going to be measuring that once a year; we have third-party benchmarks and we can measure how much clarity is there across the entire organisation as to where the heck we are going. Are our employees feeling that we are building capabilities? Are they feeling motivated and engaged. That is a really, really important voice of the employee metric. A classic other one would be health and safety, so we have a very important metric there. Then voice of the business: I mean we want to see the top line grow, so we have metrics around top-line growth and how is our top line doing versus the competition, which you would expect. How are we doing on things like EBIT growth? How are we doing on generating free cash flow? So it is very, very clear to us and those metrics are consistent across all the six business units.

Hassan Al-Wakeel (Barclays): I have a couple please. Firstly, to expand on the product portfolio question, could you be a bit more specific on your launch activity and expectations here, both on the Continence and Ostomy front? Within Ostomy, do you think we need the more 2.0, or 3.0, launches that you referred to, to stem some of the market share declines and turn them into market share gains that you have been seeing historically, or can we indeed see something sooner? That is the first.

Karim Bitar: Yeah, look, I think you have to be very practical in these situations, right? So I think it is reasonable for you to be expecting the 1.1 and 1.2 versions in the next 24 months and we just need to do that, period. I think our customers expect that and the competition is not going to wait around, right? I mean this is a dynamic race. I think that, fundamentally, to get ConvaTec on the right trajectory for sustainable and profitable growth, we absolutely have to up the ante on the innovation front. I cannot be more explicit today; it is premature. I think I would be sort of making up stories and it is just not in my nature. However, I would welcome that question again, maybe say in six, 12 months and say, 'Tell us explicitly: what is the pipeline going to look like? How is that going to happen?' We will have a chance for all of you guys to have a chance to meet with Divakar and better understand how that is being articulated. However, from a direction of travel, we need both. We cannot be waiting for the night that is going to save us in, whatever, I do not know, three years or four years; we need to do both.

Hassan Al-Wakeel: Sure. And then secondly, could you expand on the new patient trends that you are seeing here in the US within Ostomy and your expectations in light of some of the competitive wins within Acute and whether you are concerned about that?

Frank Schulkes: This is referring to the new patient starts. You used the word 'trend'. As I said in the presentation, we have seen, over a long period of time, a decline in the US NPS rates and we have seen one quarter where we have seen a slight uptick. To be honest, I am not getting too excited about it yet. It is just one quarter and it is not a trend; I think you should not, also, be getting too excited about that. We are really looking for trends and that means you need to have at least several quarters in a row where there is a sustainable type of development in a positive direction happening. I do not see that yet, so I do not have that confidence.

Hassan Al-Wakeel: Competitive wins in Acute, does that colour of how you think of the next –

Frank Schulkes: You mean the GPO, specifically? Well, as we have been very clear, our expectation has always been that this would go multi and it went multi. On top of that, it is a national contract so there are no compliance targets. In the end, like in the past, you really have to still contract with all the individual hospitals to get sales. Will our competitor have a little bit of an easier road to some of these hospitals? Possibly. However, they were contracting with some of them anyway in the past, so I do not think it is going to be a very material impact. Again, we expected it and that is what happens.

Charles Weston (RBC Capital): Hi, two questions please. The first one is on Advanced Wound Management. Obviously you said you were trying to get that growth back up to market rates. From a product-specific perspective, though, in terms of your portfolio, in the market much of the growth is coming from devices, like negative-pressure wound therapy and also bioactives and skin substitutes. So, do you think you have the right portfolio to be able to get to that market growth rate?

Karim Bitar: I will answer in two ways. I think it is clear to us that the hydrofibre segment, the negative-pressure wound therapy segment, the biologics segment, the foam segment, those are all important segments, right? I mean you can all look at the data, etcetera, etcetera. To your question of, 'Do we have the right portfolio?' I think it is fair to say that, in the hydrofibre segment, we have a pretty formidable portfolio, frankly. I think that there is room for improvement in the other segments and we are very cognisant of that. I think the positive aspect is that we are competing in the other segments but clearly, as part of the innovation strategy, we are actively exploring how can we further strengthen our portfolio? At the end of the day, yes, you want to focus on commercial execution. However, as we all know in this room, innovation is the heart of our business so we are going to need the 1.1s and 1.2s; we are going to need the 2.0s and every so often you are going to have to think of, 'Hey, here is a new offering that is not even in a segment you are currently actively working on.'

Charles Weston: Thanks. The second one, to go back to your point on staff engagement, obviously there have been a lot of changes within the business over the last few years, a lot now, you are bringing in these pillars, these sort of core beliefs within the business and it can take quite a while to implement that. Where does the staff engagement track versus industry benchmarks now?

Karim Bitar: I would say, today, relatively low would be the objective measure. What I would say is that we are very committed, as a leadership team, to improve that and I think that during the course of my visits it was very palpable to me that, fundamentally, our employees, they want to do well. Our employees want to learn, they want to grow, they want to be engaged. So, for a role like mine and that of the executive leadership team, it is a real privilege. I am actually very, very excited about all the folks that we can work with at ConvaTec. So, to me, the natural fabric, or predisposition, is actually very, very ripe. I think what is really required is a lot more clarity in terms of direction of travel, a lot more involvement of our employees. So, as we involved 900 employees in developing the vision and the core values, the level of energy and enthusiasm was incredibly high. So, objectively speaking, I would say we are starting from a low point, we are very committed to improving it and I am cautiously optimistic that we will be able to do that.

Charles Weston: Thank you.

Michael Jungling (Morgan Stanley): Good morning, I have three brief questions. Firstly, when it comes to the self-lubricating catheter, can you comment why this product is not becoming more of a push, going forward? I think there may have been some delays; can you comment on why that is? Question number two is in relation to Ostomy, can you comment on your sales force turnover in the United States today and how it compares to a year ago. Then question three is on executive leadership compensation. Can you comment on whether the targets have changed, now that you are onboard with respect to organic growth and margins, just some sort of insights into the compensation structure, thank you?

Karim Bitar: Yes, so, on the self-lubricating catheter, maybe I will ask Frank to comment first and then I will join Frank.

Frank Schulkes: Yeah. We have a self-lubricating catheter in the market, which is the GentleCath Glide and that is growing very well; it is a very good product and our customers really love it. I think what you are referring to is the compact next generation, as we call it. That is in patients in a pilot market. At this moment I really cannot comment any further on that. That is basically it.

Karim Bitar: I will just add a little bit, just to give you some colour. I think we were pretty transparent that when I said, 'Hey, three root causes,' we talked a little bit about the complexity but we also talked about some of the limited capabilities, right? Clearly, process development has been a real challenge for ConvaTec, so I think it is just important to come clean on that. We have designed, historically, some pretty intriguing offerings. In some instances we have thought about design for manufacturing, so how can I produce this product efficiently and how can I make sure that it is going to be a reliable and high-quality product? However, fundamentally, that capability is quite limited. So it is going to take some time, frankly, to sort out and say, 'Okay, A, let us acknowledge that that is a problem,' so we are in the midst of doing that. Then, B, once you acknowledge that you have a problem, I always argue that you are at least 51% of the equation there, because if you do not acknowledge it, you do not solve it, so I think we are in the midst of acknowledging that and there is going to be room for improvement. So what you see with GentleCath Air is a reflection that, yes, we are launching in a pilot market; yes, we are learning. However, not only are we learning from a commercial vantage point what makes sense but we are also learning, frankly, how do you actually scale up? So I think there is room for improvement in that arena?

To the second question, Ostomy Care sales force turnaround, Frank, do you have any insight on that?

Frank Schulkes: Well, when you think about the on the ground, feet on the street, turnover, I do not think there is a material change versus the past. However, we are changing leadership in the US specifically. I do not know if you have any further views on that?

Karim Bitar: No I would just add, look, clearly we made a leadership change for the entire global business units, so Mani Gopal has joined us. Mani is a very talented operator: he spent over a decade with Abbott and Cooper Vision, running integrated healthcare businesses and has done several turnarounds. He is an ex-McKinsey guy, spent about eight years there; he has a PhD in material science from Berkeley. I mean the guy is very, very talented; very, very capable. He has literally just been parachuted into the situation, assessing the situation. I think we were transparent as to which businesses we thought were leading, which ones were mixed and which ones were lagging. There is a lot of work to be done there and so clearly we need to focus on the US; there is a real opportunity to focus on the top IDNs, there is a real opportunity to really focus on the whole metric of new patient starts that I think Hassan may have been referring to. So, for us, it is clear what needs to get done. The reality is it is going to take a little bit of time, right, to settle down the organisation, put in place appropriate leadership. However, I think the starting point is actually pretty darn strong. I mean ConvaTec, historically, had a really strong reputation in Ostomy Care, so when I travel around and I see what we can do, I look at a market like Taiwan, right? We have shares in market north of 40%, with the current portfolio, just to give everybody a sense. Amazing engagement, hardly any turnover and we do really, really well. I look at a market like Poland; we have done really well in Poland. I look at a market like Italy, Holland. So I think one needs to be cautious and that point about mix performance really tells you that there are intersections of product and geography which would tell you we can win. Now, the question is how do we take those learnings and do that consistently? Clearly the opportunity for us in Ostomy Care is to do better in the US.

I think your last question I was going to go to was the executive leadership and compensation. Look, as a board, we are reviewing that. You previously asked me about key metrics and what we are looking for, so clearly, as a board, there is a really strong desire to reward along those metrics. Fundamentally, really the reward is heavily focused on driving revenue growth and driving earnings growth. I mean that is really what we are focused on. Then, we love free cash flow, okay? That is a really, really good measure. So if you said, 'Karim, what do you really look at?' Revenue growth, EBIT growth, free cash flow generation. We are, relatively speaking, not a very high-capital-intensity business, right? So, as you think about that, it really tells you that, hey, the margins are relatively high, compared to most industry benchmarks, most sectors. This is a business where you have to nail innovation, you have to really nail sales and marketing aspect of things and then make sure that, when you are talking about operations that the folks are efficient and can reliably, in a high-quality manner, deliver the goods. We have had a mixed record there.

David Adlington (JP Morgan): Hi, the first question is just on the 200 basis point margin for this year. The gap is quite wide; I just wonder what variables will take you towards the top or the bottom end of that range. Then, just a housekeeping question in terms of interest and tax assumptions for this year would be useful, please.

Karim Bitar: Sure. I will let Frank handle those two questions.

Frank Schulkes: Yeah. Of course, the 16–18%, a big driver of that is related to the 2–3.5% revenue guidance, or outlook, so there is a significant element of revenue performance in that. On top of that, there is a range around productivity delivery and a lot of that is TI-related. Those are the main drivers that will determine whether we are going to be in the 16% range or in the 18% range.

Tax: the tax outlook for 2020, for book tax, is around 18–19%. This is driven really by a couple of things and a lot of this is related to Switzerland and we have talked about this before. First, in about the middle of 2019, the tax holiday that we enjoyed expired. So that means that that tax rate is going up and we will feel that, of course, in 2020 for the full year. On top of that, there is Swiss tax reform, so the Swiss tax rates in general are going up. They are going to move up to close to 13% and that will happen over time but that is the second biggest driver why we see an increase from about 16–16.5% to 18–19%. Then the final one is really we are generating and creating value also outside of Switzerland and of course, when you do that, there is profit attribution to different tax jurisdictions and also typically those tax jurisdictions have tax rates that are somewhat higher than Switzerland. So that is the third element that will play a role in this increase. Longer term, very much in line with what we have communicated before, we expect book rate over the medium-to-long term, to go towards 20%, the biggest driver being Switzerland.

David Adlington: Interest assumptions?

Frank Schulkes: Well, we have refinanced our debt and we have margins between 200–225 basis points. We have a portion of our debt, we have an interest swap in place. We, at this moment, are looking at an effective rate of about 3.5%, so in line with what we have experienced before. In 2019, just to make sure that you do not fill out the wrong numbers in your models, there was an extra $11 million related to the write-off of the old financing costs related to the prior debt deal, so you have to take that out to basically go to the underlying interest rate charges. It is similar to what we have experienced before.

Scott Bardo (Berenberg Bank): You have a pretty commanding position in the supply chain of catheters in the US, distribution and homecare. It always feels to me like you have missed a trick in terms of prioritising your own product in those channels, so I wonder if you could share a little bit of thought about plans to better leverage 180 Medical and others to priority position your product?

The second question: you talked a little bit about digitalisation. I wonder whether you extend that into the product development side. It seems one of your competitors' major push is into digital ostomy bags, or sensor-based ostomy bags. Is that a market you believe in? Is that something you look to catch up on?

Karim Bitar: Yeah, so two questions. Let us take the first one on the 180 Medical; could you leverage it more? I think the short answer is yes but we need to do it right. What I mean by that is, first and foremost, we are going to take care of patients are we going to do right by patients. So what is absolutely critical is that if you or I had suffered from a very bad injury, maybe a spinal cord injury and we were going to go ahead and need the services of 180 Medical, they need to have the ability to be truly independent and do what is best for that single patient, right?

So, how can we better leverage 180 Medical? Frankly, we can up the ante on our offering, right? Because if, frankly, our offering is differentiated and unique then that makes it a lot more easy for 180 Medical to do what is best by the patient. So I think, as a guiding principle, that is really, really important. So when we talk about our five core values: improve care, that is number one. We have to make sure that that true north is there. So is there an opportunity to leverage 180 Medical a lot more? Absolutely yes but we need to do it the right way, if that makes sense.

To the idea of digital, look: you can think of digital sort of within two domains. One is within the offering, so digital is not a market, it is a big, fat word; everybody uses it today, it means everything and nothing.

When we are thinking about solutions, yes, we are thinking: can we develop smart solutions, where you take the device, you get digital and service and you integrate those three. However, you have to start out with, well, what is the problem you are actually trying to solve, right? So if, in Ostomy Care, one of the issues is, you know what, I am actually feeling very anxious and I deliberately use the word feeling 'anxious', right? I like to, personally, swim and I have often wondered. I say, 'Well, what about if I had colon cancer and I was going to go and need to swim and my daughters were there and my family and friends were there and I wanted to dive in; how would I feel?' It is beyond its functionality, right? The colour, the appearance, is it going to leak, right? There are all these thoughts that come through and so, if part of the solution is digital, to address those needs of the patient, absolutely; there is a very significant opportunity. So therefore, that is why we did recruit our Chief Medical Officer who is sort of ambidextrous in the digital world and also in what I will call the device world, similar to Divakar; these are individuals who think that way, they kind of get that.

The second area for digital, frankly, is how do you interact with your customers, right? That is a different arena; there is different media that you can use. How do you use digital to, frankly, facilitate interaction with a patient, which is very different than a traditional industrial manufacturer mindset.

So I think what I am trying to say is digital is not a marketplace; digital is a tool to help you better serve unmet needs that customers have and we need to be smart about how do we leverage digital accordingly, is what I would say.

Speaker: Thanks for taking the questions, the follow-ups: just one on SKU rationalisation. I think, historically, you have said 20% of product account for something like 95% of sales. This year you are talking about a one percentage point headwind from SKU rationalisation. Should we expect a similar headwind in the outer years, beyond 2020?

Then just a second one was on German Wound. Could you just give us an update as to what is happening there with the silver reimbursement? I was under the impression that there were some delays, or that that was not going to be happening, but have you heard something different?

Frank Schulkes: Okay. Well, on the SKU rationalisation, we are really going to seriously start that in 2020 and indeed it is a 50–100 basis point headwind for 2020, with a focus, I would say, on Ostomy but there is also, as I said before, in the CCC business and the Hospital and Crit Care business. This is not, I think, going to be over in one year, right? Implementation of SKU rationalisation and market rationalisation programmes will take some more time than just a period of 9–12 months, so I think this will also go into 2021.

On silver, we are still expecting that silver will be excluded from reimbursement in Germany and we are working with our teams to mitigate that with non-silver offerings, of course. However, we are planning that this will be a headwind in 2020 for us. There may be some delay but, at the same time, we believe that the market also will start to, probably, change behaviour in anticipation of that change.

Mark Reynolds: Okay, I think that is it. We do not have any questions on the call or the webcast so I think, with that, we are done.

Frank Schulkes: Thank you very much.

Karim Bitar: Thank you very much.

Mark Reynolds: Thank you.

[END OF TRANSCRIPT]