Edgewell Personal Care Company (EPC) | Raymond James 2022 Institutional Investors Conference | March 7, 2022

Olivia Tong:

Good morning, everyone. Thank you for joining us. Really appreciate it. I'm Olivia Tong, Raymond James's consumer goods analyst. Our next presenter this morning is Edgewell Personal Care. The company has made many changes over the last few years to better position their portfolio and improve delivery of results, and we look forward to hearing more. Joining us today in person are CFO, Dan Sullivan, and Chris Gough, VP of Investor Relations. Thank you guys for joining us. Dan will run through a few prepared remarks and then we'll come back for Q&A. Thank you.

Dan Sullivan:

Thanks, Olivia. Good morning, everyone. Chris and I are really excited to be here and share with you the story of Edgewell, which is certainly a pretty interesting one, and over the last 18 months, showing really clear signs of real transition and transformation of the business. I'll take you through that story fairly quickly. I won't spend time here, but I think we all understand safe harbor rules and guidelines.

Dan Sullivan:

There's three takeaways that Chris and I want to leave you with today. One is that this is a growing business with a very new and very different portfolio strategy. We're not a shave business that happens to do other things. We're a portfolio business that actually sees a clear path for growth, and we've demonstrated that growth over the last 18 months, with an outlook for '22 to continue the growth. So this is a growing business top line. Secondly, really interesting economics for this business and what we think is a unique business model that can drive sustained value, driven largely by two factors, both margin accretion and really healthy cashflow profile. And then third, and maybe most interesting today, is this isn't theoretical and an idea that we came up with. There are clear proof points here of how we are running this business differently and driving different results.

Dan Sullivan:

Let me talk to you a bit about top line for a minute. If I take you back two years, we had just come off a transaction that we walked away from, acquiring Harry's, and we had to develop a standalone go-forward strategy for Edgewell. We spent eight months internally with external help developing that strategy, and if I could summarize eight months' worth of work into one page, it would look something like this. I won't take you through the purpose and value and vision that we have for the business or the strategic enablers. What I will talk about, though, is how we have differentiated this portfolio to drive different outcomes. And that is basically thinking about this business through two really important lenses. One is a right to win portfolio, and one is a right to play.

Dan Sullivan:

This slide, I think, is helpful to put that picture together. On the left side of the page, you see what we consider to be our right to win businesses. Now, what does that mean, right to win? Well, these are healthy, growing categories where we have leading share positions with our brands. We have outpaced the category, so we are growing share and growing categories, and we fundamentally believe we have the right to continue to do that. On the right side of the page then is what we call right to play. This is mostly our shave and fem business, strong brands, strong share positions in markets like Japan, modest share positions elsewhere internationally, number two player here in the US. We have unique manufacturing and IP technology. These categories haven't returned to the health that we see in the other end of our portfolio, but they are getting healthier, and we are now improving our performance.

Dan Sullivan:

If you think about the right to win business, it's really made up of these three elements. Our sun care business is a source of strength for us. We have gained over 120 basis points of share in the US in the last two sun seasons. We have unique capabilities in terms of product formulation, sourcing, manufacturing. We are able to manufacturer roughly 98% of our portfolio, and we are gaining significant shelf space here in the US, particularly with new distribution that's come on board in club. So a real driving force behind growth that we think absolutely will continue as the market leader.

Dan Sullivan:

Now, the grooming portfolio is interesting, because this is actually our M&A portfolio coming to life. We have spent most of our time in sort of add-on, tuck-in acquisitions in grooming, building the number one grooming portfolio in the business. We operate across all price segments, as you see on the page. We serve very different consumer needs, depending if you're a Bulldog consumer focused on sustainability or a Jack Black consumer focused on prestige and quality. And now Wet Ones's business in the skin hygiene space has obviously benefited from recent COVID times over the last two years. That business has actually doubled. It's about a $100 million business for us.

Dan Sullivan:

And as we look forward past the pandemic, we see the real case for durable demand, based on two factors. One, the consumer continues to tell us that hand hygiene, skin hygiene will remain important to them. That trend does not go away when COVID passes. And secondly, they will continue to turn to brands they trust, like ours. So our 50% market share in the US will only grow. So that's our right to win business.

Dan Sullivan:

When we think about our right to play portfolio, again, as I mentioned earlier, this is shave and fem. Now, interesting around shave, we don't talk a lot about this, but Japan is a really interesting market for us. It's our number two market globally. It's about $200 million in annual revenue, and we are the market leader in shave. We are the Gillette of Japan. We have north of a 50 share in both men's and women's, and we act like the market leader. We price in a way like the market leader. We innovate as the market leader. We have just re-platformed the Hydro brand, brought it to shelf in October, gained distribution, and we're about to do that on the women's side. So a market leading presence in Japan.

Dan Sullivan:

The FemCare business, which is about 15% of our revenue pool, has seen some choppiness post-COVID. The category has been up and down. We're starting to see traction now in the category, two straight quarters of consumption growth in the US. We as a portfolio have grown in line with the category, so we've held share. We're in the midst of re-platforming our portfolio, simplifying it, and we're bringing new and exciting innovation to market starting later in '22.

Dan Sullivan:

And then third, but certainly not least, our women's branded shave business here in the US, where we occupy just over a 40 share of both measured and online sales. We already had a very compelling, very strong portfolio that we only made stronger with the recent acquisition of Billie. So now we are bringing to market a comprehensive portfolio, targeting obviously different consumers, operating across the full price spectrum.

Dan Sullivan:

Now let me spend a minute on the Billie acquisition, because this for us was super interesting and compelling and a great example of how we took our manufacturing capabilities, a strategic partnership as a supplier, and bought the fastest growing brands in women's shave. Billie is a DTC native business with a run rate, a revenue of about $90 million, growing at about 30%, all online. Total DTC business. A month ago, they began the journey into retail with an exclusive one year launch at Walmart. What's really exciting about this opportunity for us is not just the growth, and it will add 400 basis points of growth to our top line in just this fiscal year.

Dan Sullivan:

What's really interesting for us is the complimentary capabilities and the opportunity for the brand. So what do I mean by that? Capability-wise, we are taking the expertise of Edgewell, which is around manufacturing and retail execution, and partnering that with the most successful digitally launched brand in the space, and I'll share a bit about that in a minute. What's really exciting is, as you see how the founders built this brand, the engagement level with customers, the trust and latent equity within that brand, you can actually see this is not a shave brand. This will become the preeminent women's lifestyle brand, so you can start to see how the brand will travel across adjacent categories.

Dan Sullivan:

In terms of the omnichannel approach that I mentioned earlier, you are taking now the best of digital activation, and you can see the numbers on the page, conversion rates that are twice industry average, engagement levels above and beyond anyone else in the space, direct relationships with over a million customers, as they've acquired over two million customers on this journey, and now you're bringing this to retail. Edgewell is now the disruptor on the shelf. Full distribution in Walmart this year, tremendous in-aisle execution, signage, and displays, real stopping power, and end caps in over two-thirds of the stores. That's the program that we have now launched in Walmart. Initial results, super encouraging. We estimate that about 80% of the stores are converted. The brand has achieved a 19 share in women's shave, 1-9, in about three weeks time.

Dan Sullivan:

So you put it all together, why are we so confident and why do we have such strong conviction on top line? Because we've said publicly, we will run this business to deliver 2% to 3% organic sales per year, that is our model, through a combination of the right to win portfolio that I talked about earlier, double digit algorithm to it, and a flattish to slightly positive look in right to play. And that ambition has only been made easier with the acquisition of Billie.

Dan Sullivan:

So that's our top line. Let me spend a minute on our business model. There are really two characteristics that I would call out in terms of how we run this business and what it then creates for our shareholders. One is, we are relentless on cost. This is a journey that we started over three years ago with the Fuel program, and I'll talk more about that in a minute, but that sort of approach to cost, building into your DNA taking cost out, simplifying operations, eliminating waste, translates into healthy and growing margins. And equally, this business churns out really, really healthy cashflow, which creates tremendous opportunity and optionality for us in terms of capital allocation.

Dan Sullivan:

Let's start with the first one, around cost excellence. We have just completed the three year Fuel program where we saw $280 million of gross savings over a three year period, significantly outpacing our expectation at the time we launched the program. It was a pretty widespread effort, two-thirds of which in COGS, a third of which in SG&A. On the heels of completing that program, we then announced another two year $125 million cost savings initiative. We didn't name it. We didn't brand it. We're not going to talk about it the way we talked about Fuel, because very simply, this is how we run the business now. This is in our DNA, cost reduction, relentless on waste, driving out inefficiencies, core to who we are as a business.

Dan Sullivan:

What that has done is become the catalyst for us to deliver gross margin accretion. Now, it's not the only driver, but it has certainly been the lead driver. In addition to the cost focus, we've spent the last two years building up the capabilities and the internal database and analytics to better understand promotions, better understand trade spend, better understand the long tail of inefficient promotions that we've been able to pull back. So revenue-driving initiatives, promotions, price increase, cost-driving initiatives, Fuel, the new continuous improvement program underpins what we think is a really compelling gross margin narrative.

Dan Sullivan:

The second element of our business model is cashflow. For a business that manufactures 90% of what it sells, we actually do not have a highly capital-intense business model. It's about 3% of net sales, maybe even less in many years. We manage working capital extremely well, and so as a result, you see a picture like this. And in fact, in the last two years, delivering $175 to $190 million of free cashflow in each of the last two years, despite obviously the pandemic. What that has created for us is great optionality when we think about disciplined, balanced use of that cash and capital allocation. We will continue to invest in the business. We believe we are at an inflection point here to grow. You've heard that story already this morning. So investing in growth, R&D, innovation, in organic continues to be a primary focus for us, but it is not the only focus. This is not an "or" strategy for us, it's an "and" strategy.

Dan Sullivan:

In the last 15 months, we have initiated a dividend with a healthy 1.5% To 2% yield, 20% payout ratio as a target. And we've committed to what was an already existing authorization to buy back shares by announcing our intent to buy back $300 million worth of shares over the next three years, execution that we have begun in Q1 and accelerated now in Q2. So when you put all of that together, you're left with this financial algorithm for the business. This is how we think about running the business. We think about that 2% to 3% organic growth that I mentioned earlier. That translates to 4% to 6% in EBITDA growth and 6% to 7% in EPS growth. And that's absent of the share repurchase program. And then we again will prioritize really, really healthy cash conversion.

Dan Sullivan:

Let me now quickly jump to what we are seeing in terms of proof points. I think first, it starts with behavioral and capability. We are meshing elements of running a business that we are demonstrated good at, cost reduction, simplification, eliminating waste, I talked about that earlier, with focuses in two areas that are critical obviously to a CPG business, the first of which is innovation. We have completely re-platformed our innovation approach, putting consumer centricity at the heart of it, redesigning process, bringing in new talent and capability, shortening the cycle, and I'll show you some of the results that we're seeing as a result.

Dan Sullivan:

And we have invested significantly in the last 18 months in our digital business. We have re-platformed our site, moving to the Shopify platform, making the shopping experience more engaging, simpler, easier. We've brought in-house to our business now everything from site design to content development and copy to branding, all of those resources now internally. We've started to build up data and analytics functions to understand the DTC model better. And we are now building out capabilities across DTC, not only for our own sites, but e-retailers and Amazon as well.

Dan Sullivan:

When you look at our results for 2021, you can see, as I mentioned earlier, clear proof points of progress. I won't read through all of these. You do see the 4% organic growth. I'm going to highlight the number in the middle there. We estimate just over 70% of our US portfolio is holding or gaining share. Now, that may not seem like an overly ambitious result, but if you think about where our business was two, three years ago, that picture arguably might have been reversed. So we have steadied the business and now are holding and gaining share in the majority of our US portfolio. And in 2021, we significantly over-delivered the algorithm that I mentioned earlier, 4% growth at the top, 7% profit growth, 11% percent EPS growth, managing the business down to about two times levered.

Dan Sullivan:

But our proof points are beyond just the results, and I think if you take away one slide from this presentation, I hope it will be this one. We have significantly improved our ability to deliver innovation to the market and to win on-shelf. In terms of innovation, I mentioned earlier the re-platforming of the process. These are some of the examples of what we're bringing to market in 2022. You're seeing everything here from a re-platformed, re-architected Schick men's brand in the US. You're seeing new product innovation in sun. You're seeing actually a new razor coming to Cremo that allows us to compete at the high end of the price tier. And you're seeing the first new brand launch for us coming in '22, Field Trip, which will be a tuck-in under the Jack Black banner.

Dan Sullivan:

Equally importantly is what's happening on-shelf. For years coming out of the spin, we were losing shelf space. You can't run a business when you're cycling losses upon losses. In 2021, we stabilized that picture. We essentially were neutral on the shelf, meaning we essentially held our position for 2021. Now in 2022, we're bringing meaningful increases. Our sun business gained facings in Walmart in-aisle and better geography in Islander programs. We gained new national distribution for our Banana Boat business and club. We did the same in Wet Ones, by the way. And obviously, with the Billie's portfolio now, we have gained shelf space in Walmart in shave, but also in drug. So these are new distribution outcomes from the business that we were managing two and three years ago, again, another catalyst for the growth profile I described earlier.

Dan Sullivan:

What does it mean then for 2022? A quick word. I mean, obviously we are like everyone else operating in incredibly difficult times, challenging times, a lot of unknown. I think that's clear. I think what we will rely on is what you heard today, continuing to drive on cost, continuing to focus on productivity. Those demonstrated skills of the Fuel program and now our next round of savings come in extremely handy for us, obviously, in the environment we're in. And we've been really thoughtful on price. We have been price leading and very broad in our thinking around price in categories like FemCare and Wet Ones and shave in Japan. We've been a bit more surgical in price in US shave and sun. We are now going back with an additional round of pricing in shave in the US men's and women's branded, in grooming, and in preps.

Dan Sullivan:

So I think the balance here for us is thoughtful. We have to look beyond the near-term pressures of inflation. Obviously, we're running a business very differently with a clear goal of what we want this business to be. But in the near term, the combination of cost relief and price will help augment, to a degree, the pressures that we are facing.

Dan Sullivan:

And then lastly, what it translates to in 2022 is this picture. We will grow on growth. Our current outlook estimates about 3% organic growth on last year's 4%. We will continue to win on-shelf. We'll continue to broaden and execute around innovation. And the business will continue to be underpinned by a relentless approach to cost and strong, thoughtful cost allocation in a very disciplined way. I'm going to leave it there. I won't go through the closing thoughts. Hopefully you've gotten a new impression of Edgewell, the journey that we've been on, and the success that we've seen in this transformation. Thank you.

Olivia Tong:

Thanks, Dan. Maybe I can start sort of towards where you ended, just talking a little bit about the current environment and the geopolitical risk, volatility, et cetera. Can you talk a little bit about how you're improving your ability to navigate what obviously will likely be a more inflationary environment for some time? And then for the fiscal '22 outlook, you started a bit wider than usual, which obviously makes sense, but I assume it didn't incorporate $120 oil either. So can you talk a little bit about pricing elasticity, your views generally speaking there, and then the outlook? Thanks.

Dan Sullivan:

Sure. Yeah, look, the outlook, like many folks, carries a significant degree of uncertainty. We've tried to be extremely transparent in what we see in the cost pressures, and as you saw in my presentation, our ability to mitigate them. We have estimated about 500 basis points of inflation in the fiscal '22, and we have a really clear line of sight to offsetting about 300 basis points of that through price and cost. But we have to acknowledge we're in a really, really uncertain time. I'll give you a great example. We spent most of last year talking about resin. Resin was the commodity that drove everyone crazy. And last quarter for the first time in a year, we saw resin normalize and actually flatline a bit. In the meantime, sun chemicals popped, and every thing that you can imagine coming out of China, and now we're dealing with $130 a barrel oil prices. So we are dealing with uncertainty.

Dan Sullivan:

I think what you can rely on for us is continuing to push on cost and being really thoughtful about that. Knowing how we've done that over the last three years, we'll continue to do that. And I think on price, look, we took some really strong price increases at the start, double digits in Wet Ones, high single digits in fem, single digits in Japan shave. And as I mentioned, we're coming back in now to take further price, because the elasticities analysis for us is clear. Competitors have leaned in and moved, and we're dealing in uncharted times.

Dan Sullivan:

In terms of geopolitical, I do want to hit on the unfortunate situation that's going on around the world right now. Just to level set, first of all, on a humanitarian level, it is heartbreaking and for us obviously very disappointing to see, and our hearts and thoughts and prayers go to the people of Ukraine. We do not have manufacturing operations in the market. We have a very, very small business in Ukraine and Russia, all through third party wholesalers, completely immaterial to our business, and we've halted all shipments into the market.

Olivia Tong:

Thanks, Dan. And then just generally speaking, if you could provide a little bit more of a state of the union overall. There's been a lot of change changes over the last few years on externals, company-specific initiatives. You discussed many of the strategic changes to improve the business during your presentation. How should we be thinking about the timing of your transformation? Are you largely complete, or do adjustments still need to be made to adapt your structure, your capabilities, or even more M&A?

Dan Sullivan:

Yeah, that's a great question. I don't think we're complete. I don't know that you're ever complete in a world like this. So I would say if I had to think about it on a timeline perspective, early on. I mean, we're 18 months into this journey, but don't let early on fool you. Hopefully you saw on the presentation, we're making great progress and we're making that progress fast. I won't go back through all the elements that you heard, but you are right, Olivia. We have turned over leadership, not just at management team level, but the folks running our businesses, running our digital organization, running innovation.

Dan Sullivan:

We have invested heavily in our DTC capabilities and our brand building capabilities and how we bring innovation to shelf. And obviously, we're super pleased with how we're winning in sun and the distribution outcomes that underpin that and really, really impressive acquisitions like Billie and Cremo and the others. So early on from a timing perspective, but we think we're making great progress. And that's the view we have to look at, by the way, is beyond the current challenges we see, and are we running this business differently for a different outcome for the long term? And the answer is yes.

Olivia Tong:

One more from me, and then I'll see if anybody in the audience has any questions. On sun care, you've obviously made significant changes there, and share gains to boot, because of that. Excuse me. And it's an important part of your story this year. So can you talk about your approach to maintaining that momentum, particularly when competition picks up again? And what is embedded in your expectation for vacation demand this year, and what steps have you taken to reposition the business more towards everyday use?

Dan Sullivan:

Yeah. Look, we're super excited. 120 basis points of share gains in the US is no easy task. That momentum continued. In the first quarter, we gained 300 basis points, and in January we gained 400 basis points. Now, those are relatively small seasonal months, but momentum is certainly momentum. The other thing I think, before we talk about brands, this is a highly regulated category and we have expertise in formulation, in sourcing, in QC, efficacy of the product. You can't become a brand to consumers until you become a trusted vendor and supplier to retail, and we are, and we see that benefit on the shelf.

Dan Sullivan:

How do we continue to grow? I think there's three things we would point to. Continue to win on-shelf with distribution, and I gave you some examples of the incremental facings at Walmart, the better placement in the Islander program, the incremental distribution in club. I mean, winning breeds winning, and I think we are super excited about what we're seeing on-shelf. So that's one.

Dan Sullivan:

I think the second thing is continuing to innovate in the category and being the thought leader, with a real consumer-centric approach to what the consumer needs and how we can meet that need. And then the third thing is digital capabilities. I think we do have an opportunity to get more bang for our buck digitally, to translate our approach here into better conversion, better use of spend. I think the three of those things come together for us to help continue the momentum.

Dan Sullivan:

Last question I think you asked, how do we think about vacation and global travel? Very choppy. At this point, we're not seeing a return to holiday destinations and getaways. You're seeing pockets of it pick up. Mexico has started to show some traction, for example. Most of Asia has not. And so I would say what underpins our thinking in '22 is still a very choppy, uneven return to global travel and holiday getaway.

Olivia Tong:

Can we get a mic further down?

Speaker 3:

I was just wondering if you could walk us through how you see pricing evolving. Right now, everyone can get price, customers are accepting of it. Do you think there's an ability for you not to give that back a year or two down the road, or do you think you're going to get immediately leaned on by large customers for price reduction?

Dan Sullivan:

Yeah, that's a great question. Look, I think the easy answer here is really strong brands hold on shelf, really strong brands hold on price and don't have to, I think what you're implying is, go back into the promotional well and start to deal that back. We have no anticipation of that. In fact, our business has been managing the other way. If you look at our relative promotional spend as a percentage of net sales, we've actually pulled that down in recent years. So I'm not going to get too far ahead of ourselves in thinking about pricing down the road, but our expectation is that strong brands, of which we believe our portfolio is, have real pricing power here and that pricing power sticks.

Speaker 4:

Do you think collectively that your competitors are all going to do their best to retain price, or do you think revert back to talking about [inaudible]?

Dan Sullivan:

Yeah, look, I won't speak for the competitors, I'll speak for us. I think it's a balance. Share is important. Certainly, the journey that we've been on, we have focused almost entirely on relative performance, which is share. But price and value and how we drive revenue per item, which is something we focus on, also super important to us, whether that is driven by frontline price, which it has been in the past and will be in '22, or whether it's driven by less promotion. Our view towards our brands is a combination. Our view towards our brands is increasing revenue per unit per item and continuing to hold and/or grow share.

Olivia Tong:

Maybe one last one.

Speaker 5:

I'm just curious. If you go back a couple years, it seemed like a lot of the share gainers in your categories were these startups. The last two years, whether it's supply chain or lack of store resets, probably hurt some of those smaller companies. As things start to normalize a little bit, have you seen any changes in the customers at the retail level giving more focus back to those companies and less on you guys or the larger competitors?

Dan Sullivan:

Yeah. And I think you're speaking about shave predominantly, right?

Speaker 5:

Yeah, that would be the big one.

Dan Sullivan:

Yeah. Look, I think you're right. I think we've seen these brands come in and disrupt, gain space, gain activation on-shelf. And then unfortunately, I think typically what happens is they run into a quality issue. They run into a strength of blade issue. And there's only a couple folks in the world who can make durable, high quality, consistent blades, us and Gillette. And so once you reach that point, it's really hard to innovate in the category if you can't affect quality of shave. I think many of the folks in our space who came in with big ambition and big retailer support have hit that wall a bit, and so that's why you've seen a little bit of a return now to more of the legacy brands like ourselves.

Olivia Tong:

With that, I think we're out of time. Dan, Chris, thank you for joining us. Thank you, Edgewell. Appreciate it. Thank you all.

Chris Gough:

Thank you.

Dan Sullivan:

Thanks for your time.